# POLITICS OF FINANCIAL REGULATION

## Socio-political perspectives on (shadow) banking

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# Contents

# A – Politics of financial regulation – The ‘productivity’ of shadow banking

The ‘productivity’ of shadow banking marks the organizing power of financial interaction via and beyond financial regulation. By analysing shadow banking as new monetary institutional form, this introduction contributes to the socio-political debate on financial regulation. Whereas contemporary discussions regarding financial regulation often solely point to its efficacy, little attention is drawn on how the space off the regulatory provisions organise the financial field.

To clarify the present state of the debate, this introduction marks the limitations of research associated with International Political Economy. It displays central origins for regulatory thinking along early debates concerning information and efficiency in Financial Economics; and it contrasts this orthodoxy with the critical review by the French regulation school. To highlight the regulatory productivity of shadow banking, the article conceptualizes it as a new kind of monetary institutional form.

In conclusion, the introduction proposes a conception of financial regulation as itself a socio-political relation. This missing focus in the literature serves as the point of departure for the following socio-political perspectives on (shadow) banking

# 1. Introduction

Financial regulation and shadow banking seem to be two sides of the same coin. Indeed, analysing this relationship provides not only a perspective on their mutual enforcement, but it also mirrors political struggles more broadly (Kessler and Wilhelm 2013; Nesvetailova 2014a; Lysandrou and Nesvetailova 2015; Ban and Gabor 2016; Ban et al. 2016; Gabor 2016b; Helgadottir 2016; Murau 2017). To account for the latter aspect, this paper-based dissertation provides four perspectives on financial regulation and (shadow) banking with the common aim to better understand how, in recent years, the transnational dimension of politics has been produced and inscribed via financial practices across national jurisdictions. So far, recent studies regarding shadow banking offered a map of its 'plumbing' (Ashcraft et al. 2010), its strategic role in tax avoidance (Bryan et al. 2016), the power of its actors to capture regulation (Young 2012) and the political economics of its evolution and persistence (Gabor 2016a).

A central access point for the socio-political relevance of regulatory concerns is how knowledge is institutionalised via regulatory networks (Moschella and Tsingou 2013), procedures (Newman and Bach 2014) and organisations (Quaglia 2014). Most prominently, this can be observed with the capital standards of banks (Lall 2012; Thiemann 2014; Greenwood and Roederer-Rynning 2015; Lall 2015; Howarth and Quaglia 2016). It shows how financial practices have been (dis)associated and (dis)entangled with and from the so-called traditional banking sector, usually by taking into account new regulatory measures regarding financial innovation, technological advancement or economic globalisation (Gorton and Metrick 2010; Stein 2010; Acharya 2012; Adrian and Ashcraft 2012; Moe Grung 2012; Bengtsson 2013; Mehrling et al. 2013; Chernenko and Sunderam 2014; Plantin 2014; Colombo et al. 2016; Duca 2016).

When it comes to financial regulation and associated limitations and implementation problems, recent perspectives account for moral hazard (Hardie and Macartney 2016), regulatory arbitrage (Riles 2014), structural power (Flaherty 2015), regulatory capture (Young 2012), regulatory competition (Thiemann 2014), two-level games (James 2016), multi-level governance (Bakir and Woo 2016), lobby groups (Pagliari and Young 2016), path dependency (Schimmelfennig 2016), national perception (Munnich 2016), varieties of capitalism (Howarth and Quaglia 2016), paradigm change (Kudrna 2016a), public-private delineations (Cherednychenko 2016), principle-agent relations (Epstein and Rhodes 2016), conflicts of interest (Kruck 2016), fragmented expertise (Ziegler and Woolley 2016), policy entrepreneurs (De Rynck 2016), insider expertise (Kudrna 2016b), elite networks (Lall 2015) and coordination failure (Knaack 2015). What these perspectives have in common is their focus on how regulation is effected be it in a good or bad way. *Little attention has been drawn, however, to the productive power of regulatory texts themselves.*

If so, then such accounts tend to rely on neoliberal governance as the structural cause of the sustainability of finance-dominated politics which, for instance, emanates via neoliberal deregulation (Campbell and Bakir 2012) or, in its so-called second face, via 'reregulation as depoliticization' (Major 2012). Thus, the financial crisis may count as evidence for failed neoliberal ideals (Crouch 2011) or even epistemologies (Davies and McGoey 2012; Datz 2013); and financial reform may represent either a gradual shift in paradigms (Baker 2013a; 2013b) or a continuation of business as usual (Wigger and Buch-Hansen 2013), with similar rhetorical devices (Nørholm Just 2015), and even being reinforced by the new supervisory infrastructure (Casey 2015). These perspectives thus situate neoliberalism as either an empirical fact which can be explained via regulatory mechanisms or a causal factor for socio-political outcomes. Whereas those accounts again hold that the neoliberal paradigm in financial regulation is one of the effects, Martijn Konings (2016), for instance, enters the debate by showing how neoliberalism is able to reproduce itself via concepts such as risk and how it makes (financial) things governable (see also Kessler 2007; 2008; 2010).

In this respect, this introduction contributes to the socio-political debate on financial regulation. The article continues by providing an account of how financial regulation is approached especially in International Political Economy (IPE); it displays central origins for regulatory thinking by looking at the debates on information and efficiency in financial Economics; it then shows how even the alternative regulatory debate, instantiated by the French regulation school, is limited in conceptualizing regulation as itself a productive force. Finally, this limitation is exemplified by the problem of shadow banking as a new monetary institutional form. The article concludes with a plea to reconceptualise the study of financial regulation by also considering its own productive contingency as a socio-political relation.

## 2. Regulation and its context

This section gives an account of the socio-political debate on financial standards and regulation.[1] It provides an initial basis on which the analytical parts of the respective research papers can be placed, before giving a more specific account of the debates concerned with shadow banking and its association with the money market. Shadow banking was a central nexus for understanding the so-called Great Financial Crisis and how it relates to regulatory matters in place, plus its recent evolution as a reaction to the crisis (Hellwig 2009; Shin 2010; Deutschmann 2011; Krippner 2011; Lavoie 2013; MacKenzie and Spears 2014; Langley 2015). Indeed, regulation is not only seen as a reaction to a state of financial turmoil but may also play a part in triggering a crisis in the first place (Thiemann 2014). Another relation is expressed by the hare and the tortoise (Troeger 2014), i.e. regulation seems to be always behind the hare, whereas financial innovation functions as an already and ever-present tortoise (see also Seabrooke and Tsingou 2010).

The recent financial crisis gave the hare (again) a strong feeling of being first. After its seemingly local origin, the market interruption challenged longstanding procedures of central banks, transnational banking and international financial regulation (Yellen 2013; Borio 2014; Mehrling 2014), and called for 'better regulation' (EC 2015). The capacity to understand the consequences of financial procedures was no longer provided by routine: Economic theory failed to understand the fallout of market stability (Bryan et al. 2012; Lall 2012) and exceptional political decisions had to be taken (McCulley 2010). Academic debates within International Political Economy (IPE) reflected not only a struggle to understand the phenomenon but also triggered some reflection on how the politics of international economic relations can be analysed (Cohen 2009; Kessler 2009; Helleiner and Pagliari 2011; Germain 2013).

The crisis intervened in economic and political procedures previously perceived as normal ways for financial interactions to proceed (Best 2014). In the United States, new regulation of bipartisan support came about, the Federal Reserve used new mechanisms to stabilise the credit system and, in the private sector, new banking corporations were created, whereas others filed for bankruptcy (Maxfield 2011). In Europe, after the crisis impacted on its banks and the so-called real economy, the solvency of certain states raised concerns (Boy 2015; Langenohl 2015). Step by step, these unprecedented challenges for the common-currency area led to far reaching institutional changes(Dunlop and Radaelli 2016). New regulations, new institutions and

[1] There is a broad discussion in IPE about the problem of history in relation to a discipline and hence understanding how a discipline produces knowledge and identity (e.g. Patomaki 2009). On the problem of epistemology and its historical account see Hall (1990) and Samman (2015).

new financial as well as regulatory practices evolved (Posner and Veron 2010; Maxfield 2011; Baker 2013b; Moschella and Tsingou 2013; Mugge 2013; Rixen 2013; Newman and Bach 2014). This complex field, still in transition, has now found some reiterations of its new state.[2]

On the finance side, the new state of a volatile financial system has been associated with market-based finance or the so-called shadow banking system (FSB 2015b; Pozsar 2015; Ban et al. 2016; Bryan et al. 2016; Gabor 2016a).[3] Via the shadow banking system, the concept of credit, understandings of debt and even what is labelled as value or money appear to be different compared to more traditional understandings of banking.[4] Hence, the realm of shadow banking allowed for the production of new practices and institutions which grew to a major network for orchestrating financial flows (FSB 2015a). Financial innovations are still at the centre of the debates regarding the causes of systemic risk (Hellwig 2009; Nesvetailova 2014b; Centeno et al. 2015; Kavalski 2016; Lombardi and Moschella 2017). Practices like securitisation (Lavoie 2013; Nesvetailova and Palan 2013), products like over-the-counter derivatives (Carruthers 2013) and diverging jurisdictional contexts (Bach and Newman 2010) all point to conflict areas of private and public concerns[5] – also since the shadow banking system is not bound to political borders and, hence, represents a transnational field (Graz and Nölke 2008; Young 2012; McKeen-Edwards and Porter 2013; Underhill 2015).

The characteristics of these orders relate to political, social or economic dynamics, i.e. the respective contexts within which decisions are made, and so order is consolidated or exchange is rationalised (Langley 2004). In IPE, three distinctions to understand the regulatory context during and after the crisis can be made. First is the focus on institutions, their evolution as well as their interactions (Hall 2014; Moschella 2015); second is the growing concern with distinctive practices of especially the financial economy (LiPuma and Lee 2004; Mugge 2009); and, finally, there is the (generally more critical) focus on the root causes of financial instabilities (Nesvetailova and Palan 2013). Here, especially the latter strand complements this dissertation's effort, as it is concerned with the instability of financial markets, its constitutive conditions as well as its consequences for politics and society (Kessler and Wilhelm 2013; Bryan et al. 2016). One possible way to understand instability

[2] In Europe, that means especially the new rules for capital ratios for banks as well as the Banking Union, which put the single rulebook for European banks in place and which involves the single-resolution and supervisory mechanisms, as well as a prospective European deposit insurance scheme to come (Gros and Schoenmaker 2014; Howarth and Quaglia 2014; Spendzharova 2014; Epstein and Rhodes 2016).

[3] For an overview of the resent history of shadow banking see Lysandrou and Nesvetailova (2015) and Pozsar (2016).

[4] Or, short, what Mehrling (2012) has denoted as money-market funding of market-based credit.

[5] For a broader discussion of the private/public relation see Cutler (2003).

is to compare unstable relations to stable ones within a given system of financial order. This means, for example, to look at stable conditions as they might have prevailed during the time of the second gold standard, or the more recent so-called 'great moderation' to extract the dynamics which contributed to instability before, during and in the aftermath of crises (Boyer 2005; Dannreuther and Petit 2006; Montgomerie 2006; Engelen 2008; Erturk et al. 2008).

To complement this comparative approach, a co-evolutionary perspective stands out. This means that the instability of financial markets is very much contingent on a very specific setting of market relations (Kessler 2008; 2013). This in turn accentuates that stability and instability are in a mutual and co-constitutive relation, where the former is only understood through the latter and vice versa. This second perspective interrogates more fundamentally the autonomy of market systems via political or social constellations (Boyer 2013; Knafo 2013; Nesvetailova and Palan 2013; Palan 2013; Gabor and Vestergaard 2016). The evolving problems of such a perspective struggle more with the ends of financial markets, in contrast to fixing their means. This implies that an evaluation of regulations for financial markets refers not only to functional conditions but also to normative understandings. Reconstructing financial regulation, therefore, can highlight not only market failures and cures, but also what kind of normative framework is realised by the operations of financial markets. Especially if an event is called a 'systemic crisis', it becomes more than only a functional or legal question related to the inner workings of finance (Aglietta and Scialom 2010; Yellen 2013). What a systemic event incorporates is an exception to the rule, which makes it difficult (if not impossible) to evaluate such operations alongside legal rules established to govern the normal state of affairs (Centeno et al. 2015, 72–75).

The (international) credit system exemplifies the relation between normal and exceptional times. Its crisis brought the fragility of the market-based credit system (based on complex intermediation chains) to the fore. This system represents highly interconnected financial entities, and their interconnectedness also made them prone to the expansive (global) spread of (destabilising) local events (e.g. Thiemann 2014; Mertens 2017). To understand the contemporary relevance of shadow banking, the following two sections provide two contradicting views on how financial regulation can be conceptualized: The rise of Financial Economics after the 1970s (as a functional perspective) and the French regulation school (as a normative endeavour). Their confrontational position is highlighted via the notions of information and efficiency.

## 3. Information, efficiency and the need for regulation

This section concentrates on how two basic parameters for financial regulation evolved in Financial Economics: information and efficiency (Fama 1970; Grossman and Stiglitz 1976). From a Financial Economics perspective regulation can only restrict and provide access to information without having itself an impact on what information may tell. The existence of information stays in a neutral position. It serves as the starting point from which the degree of efficiency of markets can determined. Though both concepts, information and efficiency, represent long-lasting discussions in Economics up until today, looking at their rise in the late 1960s and early '70s, these debates provide the basic rationale of how finance should work and what regulation in this respect can achieve. It was then when the discussion around the economics of information, signals and noise emerged, and when the political idea that a government is helpful to organise fair market structures through institutions was questioned, or set aside in favour of the capacity of markets being self-sustaining. How information and markets interact, as well as how information for future investments in financial markets can be modelled, was understood through several milestones within financial economics (Fama 1970; Black and Scholes 1973; Merton 1973; Grossman and Stiglitz 1980).

A main point of critique regarding this economic fashion crystallises around the origins of a crisis. Based on the logic that efficient pricing allows for an efficient financial system under the condition of fair competition, the internal workings of finance are forced to work in optimal ways and are thus only problematic if external events or irrational behaviours affect equilibrium assumptions in rather radical ways. 'From this comes a general conception of the economy in which any form of collective organization, state intervention, or regulation inevitably becomes a cause of crisis.' (Boyer 1990, xxv)

Concepts of financial economics are closely linked with information economics. This relation is not surprising when looking at how trading in financial markets is triggered, i.e. through changing patterns of information related to markets as a whole, asset classes or individual stocks. On the one hand, the market provides information about market participants through price movements. On the other, market participants inform themselves via information which they, in turn, provide to the market. In the 1970s, theories in financial economics started to discuss the differences between perfect and imperfect information, i.e. they understood information as a definite whole which can be processed – failures could thus be specified and described via 'asymmetric' or 'imperfect' information (Akerlof 1970; Stiglitz and Rothschild 1976). This was side-lined by a discussion about the value of information and an assumption of informed market participants (Grossman 1981).

This kind of Financial Economics focused on how information and exchange relate to each other. One specific mode of this theorisation (or modelling) was organised through temporality. Time in this sense organises the problem of information, and its development – especially when projected into the future – is uncertain, and thus strategies to reduce uncertainty gain financial value. In this way, imperfect information tends to become a condition of markets (Grossman and Stiglitz 1980), rather than being a negligible parameter for understanding market exchanges. Future markets had been described as one instance of how information about the future can be integrated into market mechanisms of pricing without having only a presentist price/time conjunction. The information/time-nexus became a meta-financial product, which could also be traded in therefore created markets (MacKenzie and Millo 2003). In this sense, the quality and quantity of information became a calculative practice (Black and Scholes 1973). To be calculated though, information had to be clearly separated from noise or wrong information, as the following quote exemplifies:

> It is surely noise when a company named Computer Literacy, Inc., changes its name to fatbrain.com and its price rises 36 percent in a day, as actually occurred on Monday, March 29, 1999. (Bernstein 2007, 19)

However, this also implies that there is a grey area where it is difficult to decide if market fluctuations represent 'noisy' or 'real' information adjustments, whereby the real is then a 'true' way of representing value within markets and the noise is just false perceptions. To know everything means to separate the everything from the nothing, the information from the non-information. Both aspects are, however, important for understanding the movements of the markets, as this separation is not independent of its resulting parts. The separation of a real market value (i.e. the market as a representation of fundamental values based on all available information) from a distorted representation through noise is only valid insofar as the market becomes an object of calculation serving itself as a generator of information on future values (Merton 1973).

The calculation of future values based on experience in the form market practice had already been introduced by Irving Fisher and his work on inflationary expectations (Fisher 1930). Also here it is crucial that the past presents some evidence upon which a future outlook can be based.[6] And it is not just

[6] Indeed, the assumed hierarchy of present values over future ones closes off any contrasting assumption on probable innovation or other future profit as value even for a present understanding of possible futures. (Fisher 1930, 63–64) What follows, though, is the need to address this hierarchy

a random selection of the past but a distinctive calculation of the past that seems to be eligible to tell us something about the time ahead (Grossman 1981). Against the formation of efficient markets through costless information, Stiglitz and Grossman (1980) brought forward the argument that competitive markets only make sense 'when information is costly'. Indeed, they go on, 'whenever there are differences in beliefs that are not completely arbitraged, there is an incentive to create a market' (404).

Hence beliefs here are used synonymously with information. The politics of such a view of information, i.e. that it is related to value[7] and that it is not homogeneously distributed, gives credence to the problem that information has no firm ground but depends on availability and context. However, information is still seen as an entity that can be distributed, shared, gathered and included in calculative practices. What seems to be absent from the discussions in Financial Economics so far is that information generated within the markets is also under the condition of political and social relations, and it cannot be reduced to mechanical thinking in terms of models. In contrast, the models applied tend to substitute the socio-political contingency with methodological consistency, i.e. seeking more data that support more realistic modelling. Hence, it is quite ironic when they state that 'traders were left with differences in beliefs about the future price of the commodity. This led to the opening of a futures market' (Grossman and Stiglitz 1980, 404). Whenever an information problem persists (the very reason why there are markets), a new market is generated as a solution to the information problem so as to put in place a more authoritative entity to account for the non-solvable problem of future (information) as uncertain.

In a similar direction, a politics of uncertainty also comes to light when following Eugene Fama (1970) and the connection he makes between information and the efficiency of markets: 'A market in which prices always 'fully reflect' available information is called 'efficient'' (383). Whereas 'information' has been presented above as a central category for market organisation, the quote by Eugene Fama gives a further hunch regarding through which mode a market is governed. The notion of efficiency is used to describe and evaluate a market's performance. A high level of efficiency indicates a

via techniques of maturity transformation (i.e. insurance, hedging, central banks, states or other forms of social formation).

[7] Indeed, the practice of valuation entails a notion of politics on its own as it configures social networks via financial rationales such as calculatory practices (Chiapello 2015). Beyond that, valuation provides also a more general account to study social relations by the ones of markets (Beckert and Aspers 2011; Muniesa 2011; Lamont 2012). In this respect the politics of regulation, as put forward here, complemts these perspectives, as it reconstructs how meaning thus value is denoted via regulatory concerns.

well-functioning market, whereas a low level denotes a rather poorly functioning market. Thus, the degree of efficiency can be related, in turn, to how well available information is reflected in market prices. Fama provides three categories for information: weak, semi-strong and strong. Historical price data are denoted as weak, i.e. the most readily available; publicly available data on firms is denoted as semi-strong; and if only a few individuals have the potential to access certain information, this is regarded as strong.

Information is thus presented as a resource which can be mined, i.e. it has already been somewhere and can be discovered. The respective restrictions may generate a difference in price for information but the different constitutional forces are blanked out, notwithstanding their impact on how information is produced in the first place. Economics, in this sense, is restricted to use available data without, on the one hand, questioning their origin and, on the other, be concerned about the dynamics of their origination. The following section indicates an alternative take by the French regulation school – also here, however, regulation has its limits.

## 4. Limits of regulation

The central distinction for understanding the alternative reading by the French regulation school is its concept of regulation as a normative endeavour through which distribution is governed. Financial regulation is thus not only a tool to enable financial flows but also a political device to establish social, political and economic hierarchies. By reconstructing the counterarguments especially by the French regulation school (Boyer 1990; Boyer and Saillard 2005; Amable et al. 2010; Boyer 2010) the politics of two opposing concepts of regulation can be displayed and thus the continuum for its politics. Whereas for Financial Economics it is the markets and their efficient pricing mechanisms, which trigger limited regulatory provisions (i.e. a functional view), for the French regulation school the kind of capitalist relations and thus market formation depends on the way how government wants to regulate markets with a view on their outcomes (i.e. a normative view).

In this way, the French regulation school stands out in its account of researching history, insertions and large scale crises of *regimes of accumulation*. In contrast to the externalisation of disruptive forces as put forward by the rational expectation school, the French regulation school assumes that the origins of a crisis are a product of the respective regime of accumulation. This in turn means that the construction of institutions – the *mode of regulation* – plays a part not only in triggering a crisis, but is also useful for stabilisation or the avoidance of critical economic events. Indeed, the historically contingent and socially specific institutional form is very much part of the functioning of financial systems and conditions their relations (Jessop 1997, 504).

Between 1950 and 2000, institutional changes facilitated the consumer-led post-Fordist mode of accumulation. This model of debt-led growth that predominantly relied on the availability of credit for housing (Krippner 2011). To analyse this new system of capital, credit and risk, Boyer points to the singularity of the French regulation school being able to accomplish a shift in perspective 'from a micro-approach to regulation to a macro-analysis of the role of different financial systems in the dynamism and resilience of growth regimes, i.e. *régulation* in the French meaning' (Boyer 2010, 546). This goes beyond a flat understanding of economic relations and is best exemplified by the efficient equilibrium assumption, it incorporates the historical conditionality of the present institutional configuration, which enables economic exchange in the first place.

Thus what matter is how the 'coherence and quality [of institutional forms] contribute to macroeconomic short-term adjustment—i.e. the régulation mode—but also to long-term trends, i.e. the growth regime' (Boyer 2013, 543). The operation and connectivities of the financial system, its associated forces and functionality are a systemic expression of the *regulation mode* enshrined in the texts of its actual regulation within a transnational jurisdictional setting. To facilitate such a network, a shared understanding of how financial flows should be organised can be traced back to economic concepts, such as information and efficiency. These two notions allow for a normative framework for institutional operation and provide clues as to how and what to operate. Via a pricing mechanism, financial flows can operate efficiently and they are meant to represent the present state of (valid) information.

Whereas Financial Economics resembles a natural tool for analysing economic relations not embedded and conditioned in social relations (cf. Granovetter 1985), for the French regulation school, in contrast, it is of political origin and cocnerns what kind of *accumulation regime*[8] is installed and thus also what kind of distributional structure dominates (Hollingsworth and Boyer 1997). From a regulationist perspective efficiency is not *the* telos for market operation but an indicator of how power relations are organized within regimes of accumulation (Boyer 2000).

Petit (1999) gives an account of how the regulationist school analyses regulatory demands in relation to ongoing internal conflicts of the respective

[8] Grahl and Teague (2000, 161) provide a neat definition: 'The accumulation regime comprises the productive system, but views it in a dynamic context, as following a certain growth path linked to a given technological trajectory.'

accumulation regime, specifically, the transition period after the Fordist regime – during which the monetary institutional form changed from fixed to floating exchange rates. The respective institutional configuration is key to understanding and analysing how capitalist relations turn out without assuming 'a self-equilibrating process'. In contrast, to allow for capitalist relations to happen it 'requires intermediation from external structures'. Thus to understand economic relations as contingent and concrete social process via the 'configuration of institutional forms', (Petit 1999, 239) points to how economic relations turn out historically in their variegated form which cannot be understood via efficiency concerns (Boyer 2000, 303).

Whereas Fordism was institutionally characterised by the 'wage-labour' nexus (i.e. full-employment, social policy, job security within separated state economies) as the leading factor for economic growth (Lipietz 1997, 3), post-Fordism returned to the centrality of forms of competition (i.e. internationalisation, floating exchange rates, 'de'-regulation, new information technologies) as the central form for economic organisation – often denoted as the 'competition state' (Cerny 1997; Cerny 2010) in the era of globalisation.

Following a regulationist reading, the fall of the Berlin Wall and the rise of globalisation enforced the latter context by putting even more emphasis on competition between different kinds of capitalism (Neilson and Stubbs 2016). Thereby nationally organized compromises between capital and labour but also democracy more generally (Hirsch 1995), were undermined by 'market-led *régulation*' (Boyer 2000, 302). This specific 'mode of *régulation*'[9] not only stabilises a specific economics order but may also accentuate the internal contradictions of a respective accumulation regime. For instance, more recent studies regarding the post-Fordist debt-led growth regime show how debt-based consumption undermines the viability of its own register in the form of defaults or lost trust in the ability to repay (Stockhammer and Wildauer 2016). To reach a state where repayment is questioned on a large scale the regulatory context had first to allow for the piling-up of consumer or mortgage credit (Stockhammer 2015). A central enabling factor points to the disintermediation process around the traditional banking sector via shadow banking, as it also assembled the risk dispersion strategies in the case of credit to people with low or no regular income (Poon 2009; Seabrooke 2010).

This latter evolution is often termed financialization to accentuate that profits and economic resources are increasingly located in the financial sector (Erturk et al. 2008; van der Zwan 2014). This research perspective accentuates the financial part of the economy contrast to production in the real economy

[9] 'The mode of *régulation* consists of an assembly of institutions (sometimes 'structural forms' or 'mediations') which act to guide and stabilize the accumulation process.' (Grahl and Teague 2000, 161)

(Stockhammer 2012). This debate does indeed assemble a wide array of theoretical perspectives ranging from the French Regulation School to Marxist, Post-Keynesian and Minskyian inspired analyses (Grahl and Teague 2000; Stockhammer 2004; Lapavitsas 2011; Lavoie 2013). What these perspectives share is the assumption of the still growing importance of the financial sector for political and social matters on the micro- and the macro-levels. Whereas, from a French regulationist perspective, the respective mode of regulation and its internal contradictions explains quite well how the accumulation regime lost its viability in the face of crisis, this perspective has difficulties in understanding the persistence of the accumulation regime despite the failure of its regulatory framework. In a similar manner, the literature on financialization understands the fragility of respective growth regimes when relying on financial in contrast to other growth regimes. The stability of economic formation despite decisive interruptions of their respective rationales, is, however, little conceptualized.

Already Scherrer (1995) points to a problem, in that the regulationist tool box often assumes its own analytical categories as empirical observation. Thus, the evidence for internal contradictions expressed by crisis events should lead to a reformulation of the way in which the growth regime continues. Following the Laclau and Mauffe, Scherrer highlights the 'hegemonic' perseverance of the economic discourse that sustains the respective accumulation mode, despite its apparent failure. What is needed instead is an analysis which also considers discursive formations that provide a rationale for economic action. Thus, like Financial Economics, as outlined above, the financialization literature and the French regulation school follows economic rationales that seem to withstand analytical implications. What is proposed instead is a 'radical contingency' (Scherrer 1995, 463), and thus an openness regarding the empirical consequences of the analytical perspective.

Such a view is conceptualised in more detail in the theory part of this dissertation, along with Derrida's notion of a 'democracy to come'. Before that, however, the following section turns to a specific institutional formation that impacts on the way how the finance led growth regime is enabled and sustained via and despite of its regulation, i.e. the shadow banking system, and how it provides what is now often called 'shadow money' (Gabor and Vestergaard 2016) to the global financial system.

## 5. Regulatory politics of shadow banking

This section presents shadow banking as a new monetary institutional form, which is distinct from the system of bank-based financial exchange. Even though the money market, a key market to understand shadow banking, is used by traditional banks, their workings are still remarkably different and they have different attitudes when facing crisis. Beyond that, the money market has a quality of its own in connecting financial instruments and institutions in different ways which, via a restricted perspective on traditional banking, cannot be seen. The French regulation school (Guttmann 2008; Farhi and Macedo Cintra 2009; Aglietta and Scialom 2010; Boyer 2013) points to monetary institutional forms as constraints on money provision and credit. The recent financial crisis showed how 'other financial institutions', apart from public and private banks or pension and insurance funds, are very much part of the broader monetary institutional form.

Shadow banking turned out to be a driving force for money provision and credit, and its collapse prompted central banks and governments to consider new tools for monetary and fiscal policies to counter crisis dynamics. Even as banking and shadow banking turned out to be similar in its functioning, shadow banking's implosion displayed how they are very different from a regulatory perspective. Indeed, shadow banking, like banking in general, relates money markets and capital markets. It does so, however, by disintermediation in contrast to intermediation. Relating those two market forms comes with certain risks rooted in their respected contexts, specifically, in how they are related. On money markets, short-term securities with original maturities of less than one year are traded, whereas in capital markets, it is long-term debt instruments, i.e. original maturities of one year and more, that are traded. A central function of shadow banking is the maturity transformation though with different techniques for risk transformation. Shadow banking thus provides 'money market funding of capital market lending' (Mehrling et al. 2013; Pozsar 2014) by using derivatives as market-based insurance techniques against liquidity risk, and specific repackaging strategies and legal constructs against solvency risks (Mehrling 2012). Thus, whereas traditional banking facilitates this via its institutional capacities, i.e. capital buffers against solvency risk and deposit insurance schemes as well as their connection to central banks' lending channels against liquidity risks, shadow banking enables its functioning via market-based mechanisms.

Despite its recent appearance in the political economic literature, shadow banking as a practice of exchange existed long before the Great Financial Crisis, arguably even before institutionalized and publicly regulated banking. For instance, Walter Bagehot (1873) gave a first overview of the institutions and dynamics of the London money market from his experience gathered in Lombard Street. There, he depicted the central weaknesses of the payment system, when credit is demanded but limited and repayment is questioned. In such circumstances, he argues, the Bank of England is the only institution able to lend money, also via its relation to the political system of the

United Kingdom back then. In extraordinary times, the law which limited the money supply of Banks in addition to gold-backed paper money – the so-called Peel's Act – was broken. Bagehot points out three times of crisis – 1847, 1857 and 1866 – when the available gold reserves were not sufficient to equal the money needed to support the money markets and their associated banks.

Without suspension of the law in extraordinary times, he argues, the crises would have been more severe. Thus, money markets underscored the importance of a lender of last resort when the money supply within money markets tightens. In this way, the institutional configuration of a power a full market device to relate payments, credit and loans also impacted on the structure of its organization. It made it necessary to have a lender of last resort – the role of the modern central bank – but at the same time the interaction of money markets and their control mechanisms raises further controversies.

Hyman Minsky (1957) presents another early instance of how institutional innovation in money markets counteracts the monetary policy of a central bank. In much the same way as the shadow banking system provided low-cost funding resources, besides the traditional monetary policy sphere, he argues, the competitive character of money markets may lead to ways to circumvent interest-rate policies in favour of private credit creation: 'Once nonfinancial corporations are habituated to making "loans" with government debt as collateral, the possibility exists that collateralized loans using nongovernment paper will develop' (182). Following Minsky, 'during a long prosperity' (185), exactly when central banks try to curb inflation via their interest-rate policies, this shift is incentivised to progress.

As a result and in contrast to public credit, such private credit creation ends up being closely related to the market's liquidity conditions and thus highly vulnerable in times of economic contraction or changing expectations. This hierarchy of credit (or money) is problematic for the sustainability of money markets. Whereas central banks can replace public money for public money via their funding channels to banking institutions, monetary policy cannot easily replace private credit with public credit when need in illiquid times. Beyond that, he concludes that central banks are indeed part of financial instability as via their monetary policies, on the one hand, they trigger, on the other, institutional innovations in money markets during times of prosperity. So, while they might not be able to limit a dynamic economy, as a lender of last resort (and in the end also for money markets) central banks may prevent deep depressions.

Going back to Bagehot, also in his day, the Bank of England set the leading discount rates. It meant that no other bank or financial institution could offer a cheaper way of discounting bills: People owning bills 'seldom can get them discounted very much cheaper, for if they did everyone would leave the Bank, and the outer market would have more bills than it could bear' (Bagehot 1873, 12). Thus, the modus operandi of money markets is to find ways to employ money, not only in efficient ways but also under the condition that money is lent for a price which is to be recouped through its employment in the money market.

Modern money markets connect these forces via new forms of securitization, on the one hand; and by new forms of organization, on the other. In the money markets, instruments such as treasury bills, bank bills, certificates of deposit, commercial paper, interbank deposits, and repurchase agreements are used as forms of money to fund lending in the form of capital-market instruments, such as stocks, mortgages, corporate and government bonds (Mishkin et al. 2013, 28–29). Money market instruments provide the funding for longer-term, considered more risky though profitable, investments.

Short-term debt traded on the money market is considered to be a form of (private) money close to the non-insured deposit accounts of traditional banks (Ricks 2016, 37–42). Firms, so the argument goes, have an incentive to hold assets which, on the one hand, are close to money and liquid (as a means of payment) but, on the other, provide a higher return than cash deposits (i.e. to yield greater profits). Thus, the disadvantage of short-term financial instruments is their lower returns when compared to long-term debt instruments. Hence, there is a demand for transforming long-term, non-liquid but high-yielding assets into short-term, liquid, equally high-yielding assets. This set of interests is the basic mechanism which creates the demand for shadow banking. Indeed, '[h]olders of cash equivalents usually think of these instruments, together with currency and checkable deposits, as precisely the resources they are *not* investing' (Ricks 2016, 45).

In this way, Pozsar (2014) distinguishes four forms of money: First, pure public money consists of sovereign bonds and currency reserves (public money). Second, private-public money relates to publicly-insured deposits or the related currency denominations backed by related central banks (insured money). Third, public-private money means that trading instruments are collateralised by public forms of money, such as sovereign bonds (public shadow money). Fourth, purely private money consists of instruments collateralized by private bonds or non-insured deposits (private shadow money). He denotes the latter two instances as expressions of the shadow banking system, whereas the fourth instance functionally resembles the traditional banking system in providing not only maturity and liquidity but also credit transformation. Both latter contexts for money had, however, up until the Great Financial Crisis no sovereign backstop in place. Thus runs on this form of banking could occur, and did occur.

The system's stability before the crisis relied on the belief that pricing in liquid markets foregoes efficiently and that risk can be calculated based on past tendencies. Thus Financial Economics provided an epistemic frame work through which such a system may foster and left without regulatory constraints. Now, after the financial crisis, central banks can affect the prices mechanisms of shadow money by putting assets from the money markets onto their balance sheets. Thereby they can now set a floor for asset prices which previously was not considered to be part of the monetary policy toolbox. In this way, the evolution within money markets and their breakdown in times of stress changed the monetary system by also changing the function of the central bank. Increasingly, so the arguments by Pozsar (2016) and Mehrling (2012) go, central banks are not only liquidity providers in times of demand by specific institutions but also act as market makers in times when market-pricing does not work.

Aglietta and Orléon (1984, 233) point to this by problematizing the quantitative approach regarding money, which hides differential forms of money and especially their hierarchical relation. Combining the money view à la Pozsar, Mehrling and others with perspectives of the French regulation school opens up a view on the institutional reconfiguration of the monetary institutional form and its disassociation from national boundaries as the monetary institutional form 'is closely related to the space governed by nations and those between them' (Boyer 1990, 38). This complementary relation of shadow banking and the monetary institutional form thus provides a view on the socio-political relevance of the contemporary financial order in the context of a transnational orchestration of monetary flows and new intersections of private and public financial and regulatory institutions: a 'new normal' of shadow money (see also Gabor and Vestergaard 2016; Murau 2017).

## 6. Conclusion

This 'new normal' of shadow money, as outlined above, works as a new form of monetary constraint, it thus affects the mode of regulation and therewith the reproduction of social relations and which kind of regime of accumulation is supported. Regulation in this sense is far broader in scope than only pointing to the dysfunctionalities of a certain system in place but via its reconstruction regulations also allows to account for the socio-political implications of its evolutionary force. Beyond that, it is not restricted to national borders as monetary flows related to the shadow banking system in place also affect the international sphere of politics in coordination with investment streams. Shadow money in this sense only works in part as a 'national' money-like form. A main driver for understanding the politics of shadow banking provokes a deeper consideration of the regulatory matters governing contemporary financial relations and their evolution, which is outlined further throughout the respective papers of this dissertation. Politics, however, also deserves a more specific discussion when it comes to financial matters. Politics, in this context, is often restricted to actual decision-making regarding regulation but politics, and this is further specified in the second chapter, can also be conceptualized as part of the textual construction of regulatory matters. Financial regulation restricts and allows future matters to happen – present regulation thus closes or opens up possible socio-political pathways, e.g. in (re)directing financial flows.

Again, the social embeddedness of financial markets comes to the fore (Granovetter 1985; Swedberg 1997). Shadow banking incorporates the socio-political dynamics to account for productive forces beyond the standard concepts in economics. However, shadow banking and financial regulation provide a productive relation for organizing the financial field which is hardly perceptual via interactionist accounts, e.g. as 'global microstructures' (Knorr Cetina and Bruegger 2002). To avoid the revelation of the Parsons's Pact, i.e. the separation of economics and sociology (Stark, cited in MacKenzie 2003, 350), also the productive quality of financial regulation and, in this case, its relation to shadow banking needs to be seen as a socio-political relation.

Such a co-constitutive relation is not only central for understanding the Great Financial Crisis and the role of shadow banking therein. Since the onset of the financial crisis of 2008/9, it is questionable if the relation of the two sides (regulation/finance) of the coin have become less complex. Finance and its regulation are still framed as neutral technologies that need fixes based on their own logics. The efficiency of financial markets, for instance, is thus rather an indicator of how insulated these markets are considered in their importance for democratic decision-making or other societal concerns. Thus, also financial regulation should not only be conceptualised as a tool – be it in the end by Financial Economists or Regulationists – but itself as a productive socio-political relation.

This is the point of departure for the following articles. They show that regulatory texts offer a view on the productive socio-political relation expressed via financial regulation. The following theory paper provides a discussion of how to conceptualise politics to allow for a 'radical contingency' (according to Scherrer) – or in Derrida's words 'a democracy to come' (*B – The politics of text*). The first of the four research papers outlined below critiques an economistic reading of finance and argues for a socio-political perspective on shadow banking (*C – Heterodox economics and shadow banking*). The second paper shows how, over time, regulatory texts reframe power constellations based on the function of 'member states' of the European Union

(*D – Politics in crisis*). The third paper expands on the reflexivity of regulation and shadow banking and their dynamic co-constitution (*E – Reflexivity of shadow banking*). Finally, the fourth paper gives better insights into the processes of establishing regulation, especially regarding the (hardly possible) politicisation of alternative ideas, concerning the organisation of the financial field (*F – Limits of critique*). Whereas the first paper provides the foundational problematic regarding the missing socio-political perspectives on financial regulation, the other three papers triangulate this endeavour via a genealogical, power-related and actor-network perspective on the production of financial regulation.

Taking these parts together, analysing the politics of financial regulation provides an empirical entrance point for a more specific analysis of the evolution and present setting of political order and its social condition. Thus, the common node of this paper-based dissertation and the addressed gap in the literature concerns the production of regulation and how its production can be analysed as a socio-political relation.

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# B – The politics of text

To rethink the notion of politics and its relation to text, this paper turns to a philosophical discussion on openness under the umbrella of the ambiguous notion of ‘perhaps’. Derrida, so it is shown, outlines layers of friendship which lead him through a history of thought – a history, however, which is not actually bounded to time. It is a piece of text through which he finds his way. Thereby, he reveals the traces which connect different texts, which in turn point to a specific succession of letters. It is ‘friendship’ that serves as the focal point from which he departs with the aim to return – it is the focal point around which he steadily circulates.

This contribution first gives an overview about how text and constructivist thought are interlinked, Secondly, the text turns to Derrida’s analysis of text, as looking at its enabling condition, which is a continuous reference to other texts, and at how he reveals these references captured through the notion of the trace. Thirdly, and most centrally, this text analyses Derrida’s circular search for politics and how in so doing traces are shown and new traces are formed through the entanglement of different textual constructions, i.e. *friendship* and *perhaps*. Finally, this contribution turns to the question of whether and how politics can be understood as textual construction and what this means for further analysis.

The paper is based on (Wilhelm 2014)

Wilhelm, B. 2014. ‘Auf den Spuren Jacques Derridas: Politische Theorie als textuale Konstruktion’, in *Spurensuche: Konstruktivistische Theorien der Politik*, Martinsen, R. (ed), Wiesbaden: Springer VS, pp. 79–94.

## 1. Introduction: Politics as text

In the end, financial regulation is a piece of text. Is there a specificity to its textual condition when it comes to politics? Jacques Derrida's *politics of friendship*, so it is argued, provides an entrance point to understand the relevancy of textual construction and how politics is interwoven into this practice. The relation of text and politics is the main motivation to look deeper into the making of financial regulation and how these textual constructions stabilise and reproduce social formation on a wide-ranging scale – be it in spatial or in temporal terms. Spatially, via regulatory texts, different jurisdictions get aligned; temporally, via common rhythms, political routines provide an understanding of how to cope with future uncertainties. This discussion on the relation between text and politics, however, seeks to focus on a specific reading of the notion of 'perhaps', which is prominent in Derrida's *politics of friendship*. This notion entails the problem of how the production of text as something, which is present, leaves space for interpretation and openness in contrast to clarity and distinctiveness. What is expected from (financial) regulation is mostly the latter pair, underscored by the continuous calls for more data, transparency or simplicity. What is thereby seemingly forgotten is how these calls restrict or even exclude a concept of politics which is directed towards an unknown future, and which derives its meaning from this condition. Thus, political decisions are made in a context which cannot be known, otherwise it seems to be rather an automatism, algorithm or a mechanical understanding, in general, of social relations.

Politics of financial regulation is usually associated with perspectives accentuating either agents or structures. Lobby groups or networks can be more or less powerful given a specific regulatory concern (Christophers 2016; Newman and Posner 2016; Pagliari and Young 2016); or the dominant mode of production prioritises certain societal fractions over others (Aglietta and Scialom 2010). A new political landscape and thus views on needed regulatory concerns may be seen as guiding for change (Bell and Hindmoor 2017); or the moral context within which regulatory measures are placed may be indicative for regulatory outcomes (Orban 2016). New and often small organisations are able to produce decisive knowledge to affect regulatory rationales (Ziegler and Woolley 2016); or the confrontation of specific kinds of capitalism empowers one regulatory context over the other (Howarth and Quaglia 2016). The specific relations of powerful regulatory entities, for instance via the Bank for International Settlements and its associated central banks, may be key for policy diffusion (Andersson 2016); or technological innovation, such as automated trading, establishes new regulatory spaces that, in turn, create political struggles (Castelle et al. 2016). Specific elite networks and (Lall 2015) or dominant ideas about the way to efficiently regulate financial matters (Baker and Underhill 2015) serve as explanation for the persistence of distributional structures.

The regulatory text as itself a productive force is thus often disregarded. Even if the critical location, where regulatory texts are translated into action, is highlighted, it is human agency, e.g. the compliance officer (Lenglet 2012), which carries the situational power when confronted with ambiguity. Studies regarding financial practices which connect politics with openness remain a rare case as presented for instance along financial imaginaries (Brassett and Holmes 2016) or via foreclosing regulatory devises such as value-at-risk calculations (Lockwood 2015). To rethink the notion of politics and its relation to text, this paper turns to a philosophical discussion on openness under the umbrella of the ambiguous notion of 'perhaps'. Derrida, so it is shown, outlines layers of friendship which lead him through a history of thought – a history, however, which is not actually bounded to time. It is a piece of text through which he finds his way. Thereby, he reveals the traces which connect different texts, which in turn point to a specific succession of letters. It is 'friendship' that serves as the focal point from which he departs with the aim to return – it is the focal point around which he steadily circulates. To enable this movement, Derrida looks for traces in texts. Traces in turn inhabit a specific temporality, as they *had* been created beforehand. The trace holds on to this understanding until the tracks become covered in the present, which restarts the temporal relation as the practice of covering is in turn adding a new layer to the original trace. Traces in this sense are thus only meaningful in their distorted conservation of something which had been but which cannot fully be brought into the present. Hence, traces hold together what has passed and what is present. In a word, they 'exist' in suspension.

This contribution first gives an overview about how text and constructivist thought are interlinked (Watzlawick 1985, 10). The question is how it is possible to put text at the centre of analysis. It is argued that although practices like writing, speaking or thinking occur prior to the constitution of text, text has its own quality in building up a very specific network of signification. Secondly, the text turns to Derrida's analysis of text, as looking at its enabling condition, which is a continuous reference to other texts, and at how he reveals these references captured through the notion of the trace. This revelation shall be denoted as textual construction. Thirdly, and most centrally, this text analyses Derrida's circular search for politics and how in so doing traces are shown and new traces are formed through the entanglement of different textual constructions, i.e. *friendship* and *perhaps*. Finally, this contribution turns to the question of wether and how politics can be understood as textual construction and what this means for further analysis.

## 2. Constructing politics

The history of political thought is also a conceptual history that struggles with its constitutive concept of the political. Insofar as looking at the concept of the political within political thought is a self-reflexive as well as a self-constitutive endeavour: The political makes the political. This is, however, not a static but a dynamic process, meaning a temporal relation which might be understood as continuous circulation of political signification and thereby stabilisation. It is what, in the following, will be related to as an openness. But for now, it is about an overview of how the political can be thought about from a constructivist perspective which is twofold. On the one hand, this can point to questioning the foundations of the concept of the political; on the other, this can also point to the procedural development of the political. Thus, a constructivist understanding enables two different methodological pathways to understand the concept of the political as well as the practice of its constitution. In the following, both analytical possibilities will be discussed in more detail to prepare the ground for a discussion on the politics of textual construction.

### 2.1 Constructivist possibilities

One basic methodological distinction which is drawn in the literature is that between constructivism and empiricism. It is a distinction between the assumption that the world can be independently observed and evaluated from outside the system and, contrarily, that the world is always observed from within the system and thereby creating a constitutive interdependence of object and observing subject. This is a first reflexive layer within a constructivist understanding. The observer not only influences what can be seen and how an object is approached, but observation is also an observation of a self which is part of observational practice (cf. Schmidt 1990, 20). Through the observation, not only is the object constituted but through the relation between object and observer it is also the observing subject (e.g. observing the economy constitutes the economist). Therefore, from a constructivist perspective, observation is never a simple relation but always a co-constitutive practice of the difference between object and subject. The consequence for a constructivist analysis is therefore never to see stability but always to experience a permanent practice of (co)constitution and resolution. Even an 'epistemic solipsism', as it had been proposed (Glasersfeld 1990, 404), tends to strengthen the assumption of an independent capable observer, rather than to account for the actual dynamic at play when it comes to the practice of observation.

Derrida's understanding of text helps to find an analytical practice that not only seriously takes this dynamic interplay but also helps to go beyond (or precede) an assumption of dual observational systems, as his textual analysis points to an iterative process of deferral of the authentic but deforming text. This performative game also evokes the critique by Derrida on the Austinian (1962) performative: there is no performative that has to be actually realised beyond text in order to constitute itself. For Derrida, the performative motion remains a textual theory that does not rely on an actualisation beyond text to be successful in constituting itself. A performative relation is, therefore, not one of success or failure, and thereby assigned to functionality (cf. Searle 1975, 306–308), but relevant in its procedural formation (cf. Kripke 2006, 74). And so language games are therefore not functional relations but contingent processes steadily put forward via practices of signification. From this, a logic of difference or, in Derridaean terms, of *différance* is obtained. Steady differences of speech acts can be observed, observation itself, however, remains part of this formative (interpretative) practice.

Discussion of the political does not exclude the social, i.e. the relation of observation. One possibility to include sociality into the analysis of textual relations is proposed via the concept of translation (cf. Munday 2008, 170–172). This does not mean overcoming linguistic boundaries but rather understanding text as a steady relation of translation through observation, i.e. perceiving text. Thereby, the social is always inscribed into the textual relation.[10] The possibilities of textual structure – described in more detail below – include contingent projections (contingency meant as being within a distinctive scope in contrast to pure randomness). The translation of the social in the form of text is marked by a cutting point at which different fields of textual construction may overlap. It is exactly this situation that calls for a principle of text that has to be clarified before we can continue to follow the traces of the political.

## 2.2 A principle of text

As aforementioned above, it seems that text has a different quality to spoken language. The difference in quality points to their relation. A principle of text

[10] See how Wiechens (2002) presents the debate between Bourdieu and Derrida as well as their essays to think beyond text in different ways.

may assume that there is no hierarchical relation, i.e. that spoken language is logically prior to written text.[11] In the case of text, it is constitutive that text can relate to other texts, which relates in turn to the concept of traces as intertextual reference marking a trace that redirects to other texts, but which is never be present at the very time when they leave their marks, get erased or are overwritten (cf. Bennington/Derrida 1994, 83). In that sense, text is only insofar as it can possibly remain. Text is not contained within itself – every word, every succession of signs refers beyond a single text to other text(s). Also, the non-reference can only be thought of in relation to other text(s). Thus, what is absent is included in the present text as something absent and thus there is the presence of the absent.

This is what has been called the double and contradicting movement of *différance*, which enables us to think about the absent together with the present (cf. Derrida 2004, 120–121). The actual defers into a state of potentiality and what (analytically) remains is a trace. As far as potentiality remains – i.e. to recognise the trace as a trace, i.e. the ability to be read – that is as far as the trace declines in its actuality. This means that by reading the trace the trace gets covered, which in turn marks a new trace which is, though, still connected to the trace 'underneath'. The trace becomes absent through its presence being covered. It becomes a continuous presence:

> To the extent that every trace is the trace of a trace, no text is· "itself" enough to do without a context; but by the same token no context can really be closed, and we will read indefinitely a sentence such as "I forgot my umbrella" without ever getting to the end of it. (Bennington/Derrida 1993, 90–91)

In retracing a trace, a new trace is laid out. For a text, this means that by reading it it does not stay as it is but defers its meaning with each reading. Text exists in its own continuous. It is never in its own actual state but always presents a state of potential. It exists in its own impossibility (cf. Hoy 2000, 44). It stays in its continuous reference system and it is not able to constitute itself as present. Access to the text (through text) as well as its context (again text) is hence closed, as it is always thrown back into its condition of potentiality. Indeed, the more effort is made to see the traces, the more they vanish. Effort only contributes to the continuous reformation of the reference system. Bennington describes such a way of deconstruction as follows: It is not only about…

[11] Heidegger provides this distinction via positioning primal hearing, i.e. listening or silence as the condition of possibility for speaking (Heidegger 2001, 206–207). Text hence waits to be spoken out.

> …a "deconstructive" strategy, but a condition of thought in general. The fact that an analysis of language obliges us to treat the verb "to be" in such a way, that language thus exceeds its own resources, and especially the question "what is… ?," which grounds philosophy, implies a fold or twist in which the totality of entities is delimited, and we are no longer simply "in" language. (Bennington/Derrida 1993, 76–77)

We are within language – not in a trivial but in a fundamental sense: Language is not an eventual by-product of our speaking but is unlimited though framed in a non-actual state. For our endeavour, here this means to look at the practice of the coverage of the traces and not searching for their actual meaning. Hence, to look for the concept of the political cannot mean to perceive text as an external and silent object but as a textual construction, i.e. a self-referential and primal moment of the genesis of the political.

### 2.3 Contexts of friendship

Too much of evidence, as is noted in Derrida's *postcard*,[12] means to forget this relation of past and presence and hence that there are traces, and that only that which has left traces can still be noticed. Forgetting about their origin in turn lets us persist in the present, where everything is up front and nothing is left behind – i.e. the cards are on the table and nothing is hidden from the view of the players around it. This explicitness covers the practice of becoming. From now on, this paper follows Derrida's *politics of friendship* and its central quote assigned to Aristotle – 'Oh friends, there are no friends' – to rediscover the space explicitly hidden for politics.

The construction of this quote contains an openness in two ways. On the one hand, it is not clear if it stems from Aristotle; on the other, it has a paradoxical meaning, as it is directed towards friends but at the same time it is saying that there are none. To track the political this contribution concentrates on Derrida's discussion of the latter ambivalence with the goal to demarcate a location of the political. This location, it is anticipated, is about a moment of openness, which is assumed to be primal to the possibility of deconstruction and therefore primal to the state of final determination. This is reflected in the relation of potentiality and actuality. Politics is at play when it comes to this relation and how the transition from one to the other occurs. This space in-between is where politics can be at work before an eventual determination is reached. It is the construction of a political realm because of its possibility, i.e. a continuous potentiality and therefore a steady state to be in the realm of

[12] 'Not a single trace, an absolute camouflaging by means of too much evidence: cards on the table, they won't see anything else.' (Derrida 1987, 175)

politics. Derrida describes this as a simultaneous double movement of de-politicisation and hyper-politicisation at the same time (cf. Derrida 1996, 85).

This understanding of the political can be related to the aforementioned concept of traces. They are the practice of politics neither is based on solid ground but precisely on their own practice: traces constitute traces as politics constitutes politics. The state prior to this is the possibility to leave traces and to be in indeterminacy. For both, fundamental openness might be the enabling condition. Such an approach provides the ground for a constructivist perspective which addresses Derrida's moment of the political. This moment is marked through the condition of indeterminacy, and therefore by continuous instability. This instability, as will be shown, is expressed by the notion of *perhaps*. This textual figure focuses not on the moment of change but tries to see an event within steadiness. The quest for a textual construction related to a concept of the political is therefore about how stability is possible under a basic condition of openness: Which institutionalised collocations and contexts can be stabilised through iteration and which figures expire in a normal chaotic distribution? Derrida (1996, 83–84) describes this as follows:

> It becomes necessary to stabilise precisely because stability is not natural; it is because there is instability that stabilisation becomes necessary; it is because there is chaos that there is a need for stability.

This is not to refer to a continuous state of exceptions (as for example discussed by Agamben 1998). This contribution, rather, tries to read Derrida's politics of friendship from a constructivist point of view, which means to underline the state of openness, its relation to politics and how it might be addressed. Therefore, no signification can be assumed prior to the state of politics, be it understood as normal or exceptional – this in turn points to Derrida's notion of *perhaps*. Hence, the focus of this contribution points to the location of politics and not to the conception of politics,[13] which would mean to question existing political orders or their constitution. Such a context would already imply an assumption about, for instance, justice, as it is deeply inscribed into the different dimensions of the political realm. Deconstruction, in contrast, tries not to base its analyisis on a prior assumption of the political but to look at the motion, e.g. how justice originates (Zellinger 2003, 73). The textual construction of *perhaps* in Derrida's *politics of friendship* contains such a structuration of possible politics, which can then, in turn, be deconstructed.

[13] Contributions in this regard rather focus on practices within the political space in contrast discussing the notion of the political itself. Examples have been collected by Stocker (2007); Kern and Menke (2002) and Beardsworth (1996). In addition, Schönherr-Mann (1997) contributes to a discussion of the concept of the ethical.

# 3. A textual construction of the political

The central movement of this text – as laid out – focuses on a search for politics: What kind of textual construction is at hand if it can be identified as political? This relates to the circular movement by Derrida around the notion of friendship, which in turn *perhaps* allows for approximation. The notion of *perhaps* mentioned above is the decisive twist, when it comes to the relation of friendship, which can be marked as political. A textual construction of the political therefore concerns the positioning of friendship and how it is confronted with the notion of *perhaps*. Thus, the hypothesis of this section emerges as follows: The handling of the *perhaps*, which the trace of friendship allows, opens up a function within which the political can be placed.

To look at this more closely, three steps are presented. First, a closer look at the notion of *perhaps* is undertaken; second its relation to friendship is displayed; and finally, it is shown how a textual construction of the political thus comes about.

## 3.1 The construction of *perhaps*

Derrida warns us. He says or writes that 'one should not believe that our perhaps belongs to a regime of opinion' (Derrida 1997, 43). What kind of *perhaps* might this be? Initially, he lets us conclude that there are different spheres within which text may work. He wants us to consider a sphere which is not one of mere opinion. In his comment on Derrida's postcard, Rorty (1992, Ch. 6) points to the characteristics of a steady deferral as well as Derrida's paradoxical thinking. Rorty describes how one written work by Derrida cannot be exactly classified, or perhaps beyond that, how Derrida (or 'Derrida' as textual signification) cannot be classified; and how irony might be a way to approach Derrida. What Rorty is decisively not doing is to define this textual figure of irony. Here, Derrida works differently: Derrida shows openness by remaining open through the double movement of the interplay of *perhaps*.

The notion of *perhaps* which Derrida wants to speak about is anticipatory, it is the 'condition of decision' (Derrida 2005, 219). It is a basic potential which has to stay in its potentiality and cannot be resolved through decision. One might think – perhaps – of Heidegger's notion of openness as the condition of truth (Heidegger 1962, 355). The decision has to be constitutively a posteriori if truth – and this might be seen as 'dangerous perhaps' (Derrida 2005, 174) – has no fixation in presence, if it is exposed to historical conditions (cf. Castoriadis 2009, 239) or cannot be concluded. So:

> If there is some truth in the perhaps, it can only be that of which the friends are the friends. Only friends. The friends of truth are without the truth, even if friends cannot function without truth. The truth – that of the thinkers to come – it is impossible to be it, to be there, to have it; one must only be its friend. (Derrida 2005, 43)

### 3.2 The analogy of friendship

Derrida connects further relations in the quote above, thereby he provides a new trace and for this paper it provides the next argumentative step. Friends (in the plural) have a connection to truth, they need truth. Without truth friends cannot be paradoxically though they are without the truth – but why friends are friends with the truth? How does *perhaps* relate to friendship?

We have seen that the *perhaps* is primal to decision as well as to truth. Friendship however still lies in the dark and – at least at this point – we might not be able to fully enlighten this concept. But to anticipate the following discussion: friendship staying in its indistinctness is very closely related to the primal openness of the notion of *perhaps*. Friendship is initially a functional guide, when Derrida tries to fathom the political further. At the centre of this discussion remains the paradoxical structure of the quote attributed to Aristotle 'Oh friends, there are no friends'.[14] Or – to get more to the point – it is about to speak directly to the paradoxical itself. What Derrida finds when he tries to identify the ambiguity of the quote is the paradoxes that place themselves around the friend as a textual construction.

Aristotle, Carl Schmitt and finally Heidegger are questioned about their concept of friendship:[15] What is it – friendship? And it seems that in each of their arguments the designation of friendship is accompanied by a distinct paradoxical notion. There is the friend, who – with Aristotle – becomes someone close to a god and is thereby rather excluded from the present world. The difference between friend and enemy collapses in their co-constitutive movement, as provided by Carl Schmitt. Even though Heidegger seems to be a hard case, Derrida sees the conception of the friend as fragile when it is, on the one

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[14] One could argue that Derrida formulates this assertion (Oh friends, there are no friends) as a performative close to a prayer: 'You, my friends, be my friends. You already are, since that is what I am calling you. Moreover, how could I be your friend, how could I declare my friendship (and it consists in loving rather than in being loved), if friendship were not still to come, to be desired, to be promised? How could I give you my friendship there where friendship would not be in default, if there already were such a thing? More precisely, if the friend were not in default? If I give you friendship, it is because there is friendship (perhaps); it does not exist, presently. In any case, it is not at my disposal.' (Derrida 2005, 235)

[15] Others who were consulted were Plato, Cicero, Montaigne, Kant and Nietzsche. However, this very quick overview is only to indicate how the reconstructive manner applied by Derrida turns out.

hand, related to the community and, on the other, closely related to the individuation of being there, i.e. being with.

Hence, friendship is perhaps also an undecidedness, an openness, which is prior to the self, the own or the I? To put it more precisely: *perhaps* 'is' friendship? The text pieces we have gathered up to now shall be related to each other more decisively before we bring them closer to the political. A textual construction points to how texts relate to each other, which positions they occupy, how they do so as well as what kind of traces they allow to detect. In this sense, we have followed *perhaps* as well as friendship and we are now at the conjunction of these traces at which we can confront them. The notions of *perhaps* as well as of friendship share a primal openness. Both notions share that they inhabit the primal condition of decision before any decision. Friendship seems to be possible, its actualisation however is not brought about through a decision but through primal openness. Friendship cannot be demanded, it is not a condition, it is what may come. In the same manner, *perhaps* in a fundamental manner is what may come. Both textual constructions remain in their undecidedness.[16] This analogy might be addressed when Derrida asks:

> …is it possible to think and to implement democracy, that which would keep the old name 'democracy', while uprooting from it all these figures of friendship (philosophical and religious) which prescribe fraternity: the family and the androcentric ethnic group? (Derrida 2005, 306)

It is a double movement of giving away and occupying signification related to friendship. The notion of friendship can hold this position due to the traces left behind by friendship as textual construction.

### 3.3 The location of politics

But we are not yet at the final stage of the argument and so the last question or demand from Derrida regarding democracy has to wait. Until know we have not found a closer identification of the political. The hypothesis offered beforehand has only been partly elaborated (the handling of the *perhaps*, which the trace of friendship allows… ): The textual construction of friendship is entwined with the notion of *perhaps*. One could say the trace of friendship is thrown into *perhaps*. Now we still need to elaborate how this

[16] For this, Derrida proposes the term "telepoiesis" which combines the meaning of 'far off' (i.e. tele) with 'imaginative making' (i.e. poiesis). It is about what may come, i.e. distancing the present imaginary of the present as actuality (bare evidence) from the continuous and present state of potentiality but never put into presence and thereby far off (Derrida 2002, S. 234).

entwinement ' …opens up the function within which the political can be placed'.

In contrast to the construction of the political by Carl Schmitt, the political as understood by Derrida is not related to an entity which is constituted through and within the friend/enemy dichotomy where, according to Schmitt, the political is situated (cf. Derrida 2002, 84–85). Derrida understands the political, on the one hand, as a more abstract concept; on the other, however, he understands it in very concrete terms. The abstraction performed by Derrida goes beyond a community and beyond space and time. In this respect, the concept of the political from Derrida represents a doubling of the Schmittian potential of the political.[17] The potential of the political lies in the possibility of being with, i.e. being always and already with others. The potential of the political is not a permanent horizon of an entity as a unity but the potential of the potential. The *dynamis* is deferred into spatial and temporal infinity:

> How is this responsibility to be exercised in the best possible way? How will we know if there is *philia* or *homonoia* between us, if we are getting on well, at what moment and to what degree? How are we to distinguish between ourselves, between each of us who compose this as yet so undetermined 'we'? (Derrida 2005, 231).

The concretion, on the other hand, is the most immediate. The political does not only begin with an entity as unity but already with being and being with as individuation – within individuation itself, and hence it is more substantive than merely linked to an already present subject. The private and the public are not abstractions, which lead to an entity as unity like states, nations or people. Their difference is the innermost of the political and the innermost, or better, the *aus-einander-setzung*[18] of individuation. Derrida poses this question to Schmitt:

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[17] For Schmitt, the potential for the political lies in the real possibility ('reale Möglichkeit') (Schmitt 2002, 32–33) of the friend/enemy distinction. For Derrida, it lies in an openness expressed via his conception of the *perhaps*. This enables the Derridaean understanding to be primal in relation to the Schmittian notion of the political. The political for Derrida, as has already been shown, points to a tension of undecidedness, and thus to the potential of the potential of possible differentiation.

[18] A common translation of the daily usage of this expression might be 'to consider a subject'. To look into something, it has to be opened up and differentiated along with its pieces which make the whole. This is also what is implied by the German expression 'auseinandersetzen'. This meaning in German is, in turn, very helpful for understanding something which cannot be taken apart any further but is still present in some form and can be considered. Adding the hyphens to the expression (aus-einander-setzen) performs a double movement. At the same time, the hyphens show how the different parts of the word (which have also their individual signification) are connected and separated, i.e. they can be perceived individually as well as in their agglomeration. This specific expression regarding individuation thematises the practice of putting together and taking to pieces at the same time, whereby the practice of making (in contrast to experiencing or observing) comes to light (i.e. the practice of a 'Setzung', which means that something has been set).

> "Why does Schmitt take no account of the fact that the police and spy network – precisely, the police qua spy network […] points to what, precisely in the service of the State, ruins in advance and from within the possibility of the political, the distinction between private and public?" (Derrida 2005, 144).

The structural conditions of a difference that can become political, turns into an entity as unity as a political practice that dominates any aspect of political life. To preserve an undetermined difference, it is about retracing the movement through which perhaps friendship provides an opening for the political within which it can be placed. Going back to the notion of friendship and Heidegger, he states that…

> …*philia* [friendship] is the granting of favour. Favour gives something, which, fundamentally it does not possess but it has still to warrant so that the other being can stay within one's own.[19] (Heidegger 2001, 129)

What Heidegger expresses is the non-relationship as the relationship between friends. Friendship can thus never be fully actualised, though it has to be practised continuously as it is expected to be realised at any time – a continuous absence as presence. This notion of friendship (philia) is very close to that of Derrida when he calls for a cleaned version of friendship, i.e. its paradoxical absence as presence. Perhaps here Derrida is too close to Heidegger's thinking and it might therefore be that the 'Auseinandersetzung' with Heidegger's notion of listening ('Horchen') is part of the politics of friendship. Heidegger's notion of listening tries to formulate something primal that is prior to language, or which persists in simultaneousness. It is not meant as an antagonist to mishearing, rather it constitutes the paradoxical relation of not-yet-and-ever-since.[20] The entanglement of the *perhaps* of friendship with the political lies in the giving of the not-yet-and-ever-since.

The openness of a performative and theoretical contradiction leaves it open to the question of friendship, to point at the same time to something that cannot be created as it had been ever since being present, and to demand something that shall never come. The location of politics is the interplay – the

[19] The original German would be: 'Die φιλία ist das Gönnen der Gunst, die etwas schenkt, was ihr im Grunde nicht gehört und die doch Gewähr geben muß, damit des anderen Wesen im eigenen bleiben kann.' The translation above is my own as there is no English version of this text available yet.

[20] Heidegger positions *mishearing* (Verhören) in a similar position to Derrida and his notion of *perhaps*.

upholding of this tension (cf. Stäheli 2000, 242). Bennington encapsulates it as follows:

> This implies that politics is now, not projected into a utopian future, but in the event of the tension which is not to be *resolved*.[21] (Bennington/Derrida 1999, 257).

The commonality of *perhaps* and *mishearing* (failure to hear) lies in their unconditioned (‘existential’) openness of the textual construction. The discussion about the relation of perhaps and mishearing certainly needs greater attention; here, however, only the following quote may bring about further clarity:

> If in each case the caller and he to whom the appeal is made are *at the same time* one's own Dasein themselves, then in any failure to hear the call or any incorrect hearing of *oneself*, there lies a *definite* kind of Dasein's *Being*. A free-floating call from which 'nothing ensues' is an impossible fiction when seen existentially. With regard to Dasein, 'that nothing ensues' signifies something *positive*.[22] (Heidegger 1962, 324)

The handling of *perhaps*, which the trace of friendship allows for, hence opens up a function within which the political can be placed. This conjunction results from the analogy of the conditions of possibility by both textual constructions. The political can inhabit the tension that persists and shall persist between openness and relatedness. Derrida’s concluding demand is thus not only consequent but connects again (in a deconstructive fashion) with Aristotle and his conception of moderation:

> When will we be ready for an experience of freedom and equality that is
>
> capable of respectfully experiencing that friendship, which would at last be just, just beyond the law, and measured up against its measurelessness? (Derrida 2005, 306)

[21] And it goes on: ‘Deconstruction is not a thought of the absolute also in that one cannot absolve oneself from this tension, nor therefore acquit oneself of the indebtedness it implies.’ (Bennington/Derrida 1999, 257–258).

[22] The original German original: ‘Wenn der Rufer und der Angerufene je das eigene Dasein zumal selbst ist, dann liegt in jedem überhören des Rufes, in jedem Sich-verhören eine bestimmte Seinsart des Daseins. Ein freischwebender Ruf, auf den ‚nichts erfolgt‘, ist, existenzial gesehen, eine unmögliche Fiktion. ‚Daß nichts erfolgt‘, bedeutet daseinsmäßig etwas Positives.’

## 4. Conclusion: Textual politics

Finally, how does the path sketched out lead to political theory: What is it – political theory as textual construction?[23] The focus on the relation between a politics of friendship and *perhaps* points to how political theory is identified with the concept of a textual construction. In this respect, the following question evolves: How can textual construction be political theory? The preceding argument to substantialise the proposed hypothesis (that the handling of *perhaps*, which the trace of friendship allows, opens up the function within which the political can be placed) has tried to highlight precisely how a textual construction performs. The contribution has tried to copy Derrida into its text. Since what is the politics of friendship?

It is an essay to repeat, to deform, to multiply, to continuously touch upon a textual construction, i.e. the exclamation: Oh friends, there are no friends. In this sense, it is no longer a history which is told (the chronology of an idea) but an intersection of textual constructions, of pieces of text, whose presence cannot be fixed. They are not just simply picked up as a conglomeration of text pieces, rather each gets constructed, assembled, correlated and thereby deferred. This contribution has tried to follow this movement in order to show how Derrida entangles, constructs and composes his text pieces. Thereby, the border between reproduction and construction is emphasised to lay out a trace by following one and to construct signification by doing so. Or to say it in Derrida's words:

> The truth – that of the thinkers to come – it is impossible to be it, to be there, to have it; one must only be its friend. This also means one must be solitary – and jealous of one's retreat. This is the anchoritic truth of this truth. But it is far from abstaining from afar from the political – and even if the anchorite plays the scarecrow, such a person overpoliticizes the space of the city. (Derrida 2005, 43)

This notion of the political is thereby the precondition for another construction by Derrida: "For democracy remains to come; this is its essence in so far as it remains" (Derrida 2005, 306). It is the democracy to come, which can be found at the end of the politics of friendship. This construction in turn entails the textual construction of the political; it refers to a present practice which is in itself never present (yet) (cf. Derrida 1996, 82–83). Acting on the

[23] The problem of the concept of theory (i.e. the question about the ontology of theory) cannot be discussed in this context. However, this paper entails some consequences for such a discussion as it brings up the problem of how a theory of democracy can be conceived if the ontological status of democracy and theory is at the same level. This directs us to the general problem of separating theory and empirics, subject and object. The proposition discussed, analysing textual construction, takes on the continuous performativity of these relations as shown via the concept of a trace.

basis of *perhaps* in the form of a primal openness, a foundation without a ground, a simultaneity of different times of presence and futurity – this opens up a democratic realm.

In this way, the political is bound to an immanent form, which it already contains as a primal condition. The political in the form of undecidedness (the basis for something that in its deconstruction cannot be deconstructed further) refers to the form of the democratic. The democracy to come refers to itself and is left to steadily reiterate itself through a practice of undecidedness, insofar as the political as openness is understood through the primal *perhaps*. From the perspective of finance, it is of interest that concepts like automated regulation or the construction of risk-free assets 'overcrowd' (cf. Nesvetailova 2014) and over-determinate the time to come, and hence limit the possibilities for democracy from a Derridaean perspective. This critique is less directed towards the framing of financial policies; rather, or so it seems, it is a diagnosis of normality to reduce uncertainty by determining the time to come and hence defer the notion of politics into a presentist technocracy in contrast to a political community able to confront what cannot (or in a way should not) be known.

## 5. Literature


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# C – Heterodox economics and shadow banking

This paper positions shadow banking as a main representation of today's orchestration of financial flows not visible on the regulated balance sheets of traditional banking. Thereby, it accentuates the limitations of mainstream economics in grasping what is at play via institutional mechanisms on a global scale. Heterodox economics, in contrast, though accounting for the legal and institutional underpinnings of shadow banking's fabric, it misses the socio-political relevance of financial regulation. Theoretically, this chapter positions shadow banking as a social practice. This means that financial relations are a powerful social fabric that is, however, often evaluated based on its own terms and thus restricted from other interventions, considering for instance the social effects and origins of such a powerful and globally active financial network.

Methodologically, the chapter brings together the main regulatory and analytical approaches regarding shadow banking to show the so far limited concern of shadow banking's socio-political relevance. To pursue this argument, the first section of this paper points to the institutional qualities of shadow banking as a fundamental part of the broader financial system. The second section provides a view of the inner workings of shadow banking, which are better understood from a legal-institutionalist perspective than from a mere economic one. The papers's third section lays out the present regulatory adaptations and how they affect the current state of shadow banking. It concludes, therefore, that to understand the shadow banking system, a more fine-tuned institutional perspective must be supplemented by a perspective on the social and political contexts which condition (and are also conditioned by) the practices of shadow banking.

This paper is based on (Wilhelm 2018).

Wilhelm, B. 2018. 'Shadow Banking', in *The Routledge Handbook of Heterodox Economics. Theorizing, Analyzing, and Transforming Capitalism*, Jo, T.-H., Chester, L. & D'ippoliti, C. (eds), Abingdon: Routledge, pp. 264–275.

# 1. Introduction

The shadow banking system offers at least two insights into the legal underpinnings of the financial system. On the one hand, shadow banking operates on a global or transnational scale, which makes it difficult to relate it to a single national legal framework. On the other hand, shadow banking displays the effects of an ineffective legal framework when ‘adverse’ economic conditions arise. The Financial Stability Board defined shadow banking “as the system of credit intermediation that involves entities and activities outside the regular banking system” (FSB 2011a: 3) and it has been described as being “at the heart of the credit crisis” (Pozsar 2008: 17). The systemic importance of shadow banking for global finance came to light during the financial crisis of 2007-08. Paul McCulley, who first coined the term shadow banking in 2007, refers to the balance of private and public forces that were distorted before and during this financial crisis. Since then, regulators have endeavoured to rebalance the banking system (IOSCO 2009; BCBS 2011; Bakk-Simon et al. 2012; IMF 2014; ESRB 2015; FSB 2015a).

Economically, shadow banking performs banking-like practices; legally, however, it holds a privileged accounting position that comes with lower or no capital requirements compared to the traditional banking sector (Ordoñez 2013; Plantin 2014; Ferrante 2015). Hence, a purely economic analysis is limited if seeking to understand the role of shadow banking. Instead, exploring the interplay of financial regulation and shadow banking activities will paint a more comprehensive picture of the institutional evolution of the financial practices that stabilise and destabilise the financial system.

After the so-called run on the shadow banking system in 2008, the integration of shadow banking practices into the regulatory frameworks has been much discussed (Joint Forum 2008; IOSCO 2008; BCBS 2009; FSB 2011b). While the Financial Stability Board (FSB) and others support “non-bank financing” as it “provides a valuable alternative to bank funding and helps support real economic activity” (FSB 2015b: 1). However, the question of what this actually means for rebalancing the financial system is still debatable; as highlighted by McCulley, the question is one of if, and how, shadow banking can function in its tamed version.

This chapter illuminates the practices and regulatory aspects of the workings of the shadow banking system. The first section of the chapter points to the institutional qualities of shadow banking as a fundamental part of the broader financial system. The second section provides a view on the inner workings of shadow banking which are better understood from a legal perspective than from an economic one. The chapter's third section lays out the present regulatory adaptations and how they affect the current state of shadow banking. The chapter argues that, in order to understand the shadow banking system, a more fine-tuned institutional perspective must be supplemented with a perspective on the social and political contexts that condition (and are also conditioned by) the practices of shadow banking.

## 2. Institutionalising shadow banking

The inclusion of shadow banking in regulatory regimes impacts on how intervention in economic systems is practiced (Bundesbank 2014; Pozsar 2015). This, in turn, creates a new mode for governing international financial markets that further increases the homogeneity of financial practices and the interconnectivity of risks (Shin 2009). The crisis of 2007-08 further underlines the importance of shadow banking for the functioning of the internationalised capitalist system. Its collapse, starting with the Lehman Brothers' failure in 2008, indicates the interconnectedness of financial institutions and thereby the systemic vulnerability of the international financial architecture.

Mainstream economics has retained its unquestioned explanations of the present position of shadow banking—greed, moral hazard, asymmetric information, lack of transparency, and false regulation. Hodgson (2015), however, suggests that in terms of the broader working of capitalism, it is the institutional environment of shadow banking that affects the very practice of financial exchange. Beyond the financial sector, shadow banking influences political and social relations. Shadow banking had not only enforced a 'homeowner society' via the repackaging of mortgages into saleable assets but also further integration of financial institutions at the global level. Consequently, shadow banking introduces additional systemic risk (embedded in new forms of credit and in collateral provision across state borders) that calls for new regulatory measures if such risk is to be contained.

Heterodox economists generally do not limit their analyses to only economic phenomena. Heterodox economic analyses of finance are situated within the social and institutional context, including social norms and sanctions. The legitimacy of these institutions is represented through regulatory regimes as the basis for financial interaction. Financial interactions are increasingly less contained within national boundaries; hence they must be governed by complex international regulatory mechanisms. Thus, to understand financial interaction within and beyond state-based legal frameworks, one has to understand the international regulatory relations, which have recently been broadened and, consequently, created new forms of 'financial innovation.'[1]

Especially post-crisis regulatory measures show a tendency to enhance resilience to crises, rather than to focus on specific risk characteristics and hedging strategies. Their focus places greater emphasis on bank equity than on external ratings, and more reliance on trading through third parties (that is, clearing counter parties) than on bilateral inter-bank markets (that is, over-the-counter transactions). This emphasis on resilience indicates that crises are increasingly recognised as a common phenomenon. Such recognition is considerably different from the widely-accepted view represented by the applied risk models that dominanted before the recent global financial crisis. Thus, the rediscovery of the 'Minsky moment' (BIS 2008; Nesvetailova 2014; Ordoñez & Gorton 2014) reconfigured the way in which possible futures can be conjectured in an economic and regulatory sense.

In addition, the 'Bagehot moment' (Mehrling 2012) marks the decisive position of the central banks during the collapse of the shadow banking system. The new state of financial affairs created through regulatory reform places pressure on the normal business behaviour not only of banks (and the configuration of their financial assets in line with the new regulatory demands), but also of central banks (CGFS 2015). Especially for central banks in the face of a low interest rate environment, financial regulation seems to be a key instrument to adjust the lending behaviour of banks and the economy at large.

This new dynamic components of regulatory control provide, amongst other mechanisms, new tools to govern financial affairs from a regulatory perspective. From this point of view, the new role of the European Central Bank as the main agency for European banking supervision appears to be a logical step towards adopting the 'new normal' in economic governance from a distance (Mehrling 2012, 2014). The new configuration and transmission of central bank policies have thereby expanded and become more complicated. These new policies might thus more closely resemble adjustable tools vis-à-vis the developments of a future shadow banking system.[2]

In the past few years, some heterodox economic perspectives have developed ways to analyse the financial system based on Schumpeterian (Ülgen 2014), Kaleckian/Minskian (Wray 2009; Ryoo 2013; Fisher & Bernardo

[1] Financial innovation can not be reduced to individual financial products; rather, it is the way in which financial flows are reconfigured and thereby create new connections between financial products and new organizational nodes (i.e. financial institutions organizing exchanges). For a more detailed explanation see Guttmann (2016: ch. 5).

[2] One should not overlook the increasing involvement of central banks in financial exchanges as a counterparty connected to a greater number of financial institutions; and also via their balance sheets and the assets covering a more extensive spectrum of involvement.

2014), or more general Post Keynesian (Guttmann 2012; Lavoie 2013) models. Ülgen (2014), for instance, places an emphasis on the self-reflexivity of the financial system ('finance to finance' versus 'finance to production'), which disputes the unquestioned role of banking as a functional step to finance Schumpeterian innovation. A Minskian perspective of unstable capitalism, he argues, allows a better perspective on the destructive capacities of finance.

Wray (2009), draws on Veblen to explicate the transition from commercial to financial capitalism (Minsky's money manager capitalism). He argues that, in the present system, private debt plays the leading role for economic growth, and securitisation becomes central to the mode of accumulation. Post Keynesians present a more systemic perspective on the present accumulation regime denoted as 'financialisation' (Lavoie 2013). Since the 1980s, neoliberal policies, such as deregulation, privatisation, the intensification of competition, labor market flexibility, have restructured the economic system in favor of money managers.

One point of commonality between these heterodox perspectives is the rejection of the market efficiency theory formalized by Fama (1970, 1991). Moreover, heterodox analyses of the crisis demonstrate that even a broader understanding of economics might be insufficient to understand the setting of shadow banking in the contemporary mode of accumulation with an increasingly homogenous global regulatory setting becoming evident. Complementing an economic perspective, the question that arises from a socio-political viewpoint revolves around the way certain financial orders flourish and others do not, independently of *a posteriori* rational explanations, and how political decisions regarding regulation trigger further evolution of the financial system.

Shadow banking is not only an impediment to better economic governance or regulatory systems. Both aspects suggest the need for interdisciplinary research by heterodox economists, financial lawyers, sociologists, historians, and political scientists. In this way, shadow banking can be understood as an effect of a socio-political system, demonstrating how a value system transcends national boundaries and how its institutions provide for financial flows accordingly. In the present low interest rate environment, the 'search for yield' does not only challenge the current regulatory space but also resets such socio-political 'normality.' It provides a new regulatory context for banks as well as for the insurance market or syndicated leveraged loan market (Lysandrou & Nesvetailova 2014; Joint Forum 2015). Financial investors have to adjust their balance sheets and product portfolios. Such an adjustment changes not only credit availability for the 'real' sector of the economy but also financial flows of large institutional investors.

The changes in international regulatory frameworks for banks are well represented by the transition from Basel II to Basel III. Basel II provision only cover counter-party risk and accentuate the internal governance of financial institutions. Basel III focuses on 'credit value adjustment' and encompasses broader market fluctuations such as consumption, industrial production, and foreign exchange. As demonstrated by the recent financial crisis, value adjustments for whole asset categories (for valuation dominantly performed in the shadow banking sector) can cause even more systemic interruption than the actual defaults of specific assets. The crisis effects of mark-to-market valuation[3] may increase due to the growing need for interest bearing assets and hence new forms of collateral. This also reflected in that securitisation remains the dominant form of market based credit provision (BCBS & IOSCO 2015).

'Efficiency' in regulatory terms denotes the need to pursue maturity transformation off-balance sheet in order not to be subject to higher regulatory capital ratios. Banks can outsource an established cash flow and free their balance sheet for further investment (Gorton & Souleles 2005). The interlinking of special purpose vehicles solved this problem. They also allowed for an expansion of seemingly secure assets backed by seemingly reliable hedging strategies based on 'normal' probability distributions of future events (Merton 1974; BCBS 2005). The bankruptcy prone off-balance sheet construction of the shadow banking system failed when the banks rescued their sponsored special purpose vehicles (SPVs), more out of fear of losing further credibility within a tumbling financial market than because of contractual obligation. Exposures to special investment vehicles (a type of SPV) shrank from $297 billion in 2007 to $45 billion in 2008 (Joint Forum 2009).

The image of shadow banking as a 'money market funding of capital market lending' (Mehrling et al. 2015) suggests an abstract understanding of the cash flow across traditional and shadow banking institutions. Indeed, shadow banking is often presented as the other side of banking, although it is the largest (investment) banks that make broad use of arbitrage opportunities via the cash flow structure of the shadow banking system (Joint Forum 2009, 2015).

Mehrling's (2012) inclusive vision of a functioning market-based credit system misses the reality of a global regulatory structure not backed by a sovereign entity such as a self-contained nation state during the post-Second World War period of the last century. The next section sheds more light on

[3] Mark-to-market accounting is an asset value measurement method based on current market prices that directly link market volatility to balance sheet exposures, such as securities for trading purposes. This means that capital ratios have to adapt to current market conditions, and there has to be a market for such financial products in order to generate a market price—both aspects are critical for the soundness of financial institutions in the contexts of market turmoil or crisis.

how shadow banking can be explained and understood in a different way, focusing on the legal structures that enable and restrict certain cash flows or privilege particular financial products.

## 3. A legal view of shadow banking

After the global financial crisis, the G-20 (2010) called for a tighter regulation of the shadow banking system, as it was marked as a primary source for the global spread of financial turmoil. The Financial Stability Board (FSB 2011b) is the main forum for setting the regulatory agenda for a more stable international financial architecture. Together with the Basle Committee on Banking Supervision (BCBS 2011) and the International Organization of Securities Commissions (IOSCO 2009), the FSB is to provide the means to rebalance and thus stabilize the architecture of the international financial system.

Even though the FSB took up the new notion of shadow banking as brought forward by the G-20, issues such as securitization (Plantin 2011), special purpose vehicles (Gorton & Souleles 2005), off-balance sheet activities by banks (BCBS 1986) and the associated systemic risk (Hellwig 1995), and macro prudential regulation (Borio 2005) had long been discussed before the crisis. The new notion of shadow banking—non-bank intermediation chains for market based credit provision—served as a node for a widespread regulatory agenda (FSB 2013). Research on re-intermediation practices (Rajan 2005), mark-to-market accounting (Plantin et al. 2005, 2007), and credit ratings thorugh value-at-risk calculations (Fender & Kiff 2004) has highlighted in detail the systemic challenges posed by what is now called shadow banking.

Shadow banking is commonly defined as non-bank intermediation[4] (FSB 2011b). What distinguishes banks from these non-banking entities is that they have no direct access to central bank liquidity; nor are they secured through a deposit insurance scheme. Hence, the run on the shadow banking system, which came to its height around the Lehman failure in September 2008, was fostered by the knowledge about the lack institutional resources in times of crisis. It is thus commonly acknowledged that the trigger for the financial crisis was very similar to those associated with traditional banking crises, in the light of which deposit insurance and the lender of last resort

[4] Often this practice is also understood as dis-intermediation or a market-based credit system, as the main intermediaries between creditors and debtors (banks) are not directly involved. For the purpose of creating products suitable for a market-based credit system, such as Mortgage Backed Securities, the original mortgage contract has to pass thorough several legal entities that actually extend the intermediation chain.

function (meaning modern central banks) were put in place (Brunnermeier 2009; Moe 2012).

The shadow banking system relies on mainstream financial economics offering mathematical models to transfer the risk, for instance, of maturity or liquidity transformation (Bouvard et al. 2015). Maturity transformation practiced by banks means providing long-term loans and financing them through short-term debt. The shadow banking system performs a similar function although in reverse order and without the regulatory cushion. In order to reverse the maturity order, debt is transformed into a standardised category backed by risk calculations, credit insurance, collateral pools, and credit ratings. Thereby, long-term credit like mortgages can be transformed into well-tradable assets. Such a market-based credit system transfers (at least in theory) the attached risks directly to the holders of these assets (often banks themselves), without the traditional banking sector as an intermediary.

Legal entities, sometimes called SPVs or Other Financial Entities (OFEs), form a chain of different functions through which investors and creditors can be linked to the traditional banking system and thus to the traditional back-up systems and regulatory obligations. Investments in the shadow banking system hence do not work in the 'boring finance' way—whereby banks hold low interest-bearing deposits or government bonds through which they leverage their investments in higher interest-bearing longer term credit portfolios. Rather, shadow banking can be understood as an off-balance sheet arrangement, which fosters and promotes new practices of securitization.

Thus, the 'shadowy' part of banking stems from directing financial flows through non-bank financial institutions, where the whole setting is mainly created by banks that charge for its use but have no legal responsibility for its sustainability.[5] It is the legal structure which enables (or does not forbid) what can actually be originated, sold and then included in the respective capital structures. Here, Hodgson's legal institutionalism therefore directs us to 'a disaggregated view.' In this respect, Lysandrou & Nesvetailova's (2015) recent study provides a better understanding of the practice of shadow banking than the aggregation of monetary amounts that arguably represent the shadow banking system. As evidenced by Pozsar *et al.'s* (2010) mapping exercise, shadow banking is a way to legally enable certain financial products, which in turn interconnect the financial system in critical ways. These cannot be understood by looking purely at the size of monetary aggregates.

As such, the institutional financial structure allows the shadow banking system to create highly rated short-term products with interest rates above

[5] Money Market Mutual Funds, for instance, had been main drivers for repackaging mortgage loans into differentiated securities, as they provide an alternative to government bonds in terms of the probability of default assumptions though promising higher returns.

those of government bonds and significantly above the interbank rates, which is of interest especially to money market mutual funds (Bengtsson 2013; Chernenko & Sunderam 2014). The shadow banking system is able to absorb long-term or lower-rated products that increased demand for debt to be securitised; in fact, it established a fee-based originate-to-distribute arrangement through which earnings can be realised via transferring, for instance, default risks to investors (Brunnermeier 2009).[6] Consequently, the system enables banks to manage their balance sheet in a way that makes it more 'attractive' for their shareholders (FSF 2008). This arrangement can also abate the high-risk appetite of other institutional investors through its ability to differentiate risk exposures. The main way to achieve this is through a mixture of risk mitigation strategies such as liquidity facilities, credit default swaps or cash-flow waterfalls, which resulted in 'pseudo-risk-less' (Stein 2010) securities being safe in the good times but very risky in the bad ones.

Securities—collateral backed financial instruments—function as a form of money within the shadow banking system through which one is able to gain income in the form of interest payments correlated to the risk one is willing to take. Standard securities enabled the pooling of multiple loans; this strategy has the benefit not to be exposed to total failure if a specific credit cannot be serviced. The second layer of securitization, the securitization of securities or so-called collateralised debt obligations (CDOs), provides risk stratification through trenching—that is, the creation of a so-called waterfall of cash flow from the upper tranches to the lower ones from which the calculated proportion of creditors can service its payment obligations. In the case of losses, this means that cash flows related to the securities will first serve the upper tranches (super senior or senior), before trickling down to the intermediate (the mezzanine tranche) and finally to the lowest positioned tranches (called junior or equity). In addition, and in order to further reduce risk exposures, financial innovation provides credit insurance for special investment vehicles and security tranches in the form of credit default swaps. In this way, insured upper tranches could receive the highest (triple A) ratings, whereas other tranches could satisfy the hunger for higher returns (mezzanine tranches with B ratings, or unrated junior or equity tranches). Though usually only very secure assets are assigned the lowest default probability, based on such financial

[6] The move from an originate-to-hold to an originate-to-distribute business model also marks the changing incentive structure for risk evaluations. There might be a greater incentive to look at the underlying collateral if banks want to hold a credit they originated and hold to maturity than when they never hold the asset but only orchestrate its legal manufacture. In the latter case, profit does not arise from interest but from fees, which encourage an expansion of the financial manufacturing industry, that is, shadow banking.

engineering, securities based on subprime mortgages can receive the highest triple A credit rating by the dominant rating agencies.[7]

This 'entanglement' points to the need for comprehensive regulation that does not predominantly rely on credit ratings. In the context of systemic disruptions, a change in credit ratings has effects similar to those of mark-to-market accounting, creating a high demand for liquidity in non-liquid times. What has actually been created is an enlargement of the capital basis for banks along with opaque legal entities involved in creating financial products in order to hide their financial relations to banking institutions. The next section turns to the regulatory debate about shadow banking.

## 4. Regulatory reform and its consequences

As outlined above, shadow banking provides a new way to create debt in a seemingly very profitable and, at the same time, low-risk way, at least as long as most parts of the financial system remain intact. However, as indicated by the Asian Financial Crisis and the failure of Long Term Capital Management, an emergence of 'super portfolios' disrupts the effectiveness of hedging strategies (see MacKenzie 2003), especially if a seemingly highly improbable event challenges the financial order systematically. CDOs, for instance, can be highly efficient if the financial system complies with the projected risk trajectory, assuming that systemic events might happen once in a 1000 years (implying that a financial system would last that long and that the single event could be imagined at a similar distance from present times). The watering down of eligibility criteria for individual creditors and financial product has been long ignored. The systemic success of shadow banking produced new risk configurations through massive supply and demand for private debt—a self-reinforcing effect that should have been prevented already by the pre global financial crisis regulatory framework.

Considering that activities pertaining to the shadow banking system "often generate benefits for the financial system and real economy, for example by providing alternative financing to the economy and by creating competition in financial markets that may lead to innovation, efficient credit allocation and cost reduction" (FSB 2012: 3), ex-post regulatory proposal can also be read as a blueprint to enable such intermediation chains and risk mitigation strategies.

[7] The role of credit rating agencies in misrepresenting the actual risk of structured financial products should not be understated, though there is a broad discussion about their role in generating the crisis dynamics through their conflicts of interest in the rating of financial products by the institutions that profits from higher rating results. This chapter however discusses more specifically the internal function of shadow banking.

The Basel framework for banking regulation interconnected the international banking system more closely by providing common standards, especially for capital requirements and capital transactions. Consequently, securitization can be pursued within an internationalised market through a common understanding of risk, allowing for the decreased hindrance of financial exchange by national borders. The different jurisdictional provisions concerning banking enabled a practice of cherry picking the most suitable legal framework for enhancing and modifying the respective business strategies of financial firms.

As the Joint Forum (2009: 18) highlights, “because the Basel II framework is more risk sensitive, it is likely to have a material effect on bank investors in terms of their interest in various types of securities.” The heightened sensitivity of financial regulation compared to the Basel I framework for financial practices created incentives for the increased compliance of asset portfolios with the risk hierarchies implemented via Basel II. What looked like a success for the regulatory process, however, turned out to be a trigger for demands for tailored investment products suitable for the respective risk portfolios of banks and provided by shadow banking, which thus became an incremental part of global financial intermediation (Plantin 2014).

One driver of this change was the inclusion of a portfolio invariant risk conception into regulatory standards. This established a singular understanding of risk, meaning that risk could be calculated and compared independently of its spatial, temporal or institutional origin (Kessler & Wilhelm 2013). Thus, “diversification effects would depend on how well a new loan fits into an existing portfolio” (BCBS 2005: 4). The portfolio in question is made up of risk-weighted assets, which undergo a mark-to-market valuation. In this way, banks are asked to manage their balance sheets according to market variations in a shared governance system in order to keep up with regulatory demands concerning their respective capital requirements.

Credit ratings for financial institutions and products functions as a widespread standard according to which the risk structure of a bank’s balance sheet can be calculated. When market developments are retained in the projected range of risk frames, credit ratings provide the ‘facts’ that “suffice to determine the capital charges of credit instruments” (BCBS 2005: 4). The underlying formulae to calculate the needed regulatory capital contain, however, several assumptions about the functioning of markets (for example, differentiated risk weights for sovereign bonds and car loans). After a crisis, however, these assumptions seem to apply only if ratings had not been built into financial instruments, thus aligning the balance sheets of banks to regulatory requirements and potentially providing for a shared crisis trigger when ratings for product categories change.

One assumption intuition built into capital requirements calculations is that capital charges for long-term obligations should be higher than for short-term exposure. Lower capital charges for short-term investments and similar investment strategies create investment incentives and, thereby, demand for such products not only from money market funds. The business model of shadow banking is exactly to provide an 'efficient' maturity transformation, This, in turn, stimulates the need for (seemingly less risky) short-term debt leading to an increase in the roll-over of long term investments through the issuance of short-term securitized debt. To do so, the shadow banking system makes use of collateralised liabilities which could be produced more 'efficiently' off the traditional and regulated banking sector's balance sheets (Plantin 2014).

Still needed to create such money-like securities is a high degree of standardization, that is, a high degree of information insensitivity paired with broadly accepted standards of transparency. Both aspects are achieved through the regulation of risk weights according to securitization categories (especially asset classes such as securities backed by prime mortgages), as well as external ratings as provided by credit agencies. This combination creates an 'opaque' and, at the same time, clear basis for investment decisions in favour of asset backed securities and securities thereof (Gorton 2015).

There is a sense of there being enough information about abstract categories like a senior tranche of a mortgage portfolio, as well as a sense that the construction of structured investment products is immune to detailed disclosures of the performance of singular mortgages. Thus, the rollover risk created through the transformation of single mortgages with long-term maturity into short-term securities could be eliminated, especially via the use of 'risk neutral' special investment vehicles. Only through such a legal structure can the exchange of collateralized financial products function in a money-like fashion.

Although trust in, and the liquidity of, shadow banking practices has vanished, regulators across the globe still try to refine the legal structure to make market-based banking more resilient (ECB & BoE 2014; ESRB 2014; FSB 2015a; BCBS & IOSCO 2015; IMF 2015). These efforts commonly agree in the provision of more granular data about distinctive investment products, as well as the need to better understand how financial institutions are linked. Therefore, the importance of central clearing counterparties has risen due to further adjustment of the Basel scheme (BCBS 2011). The calculation of risk is now related to how banks interact ('inter-connectedness'), to their lending along economic cycles ('pro-cyclicality'), and to their indebtedness ('leverage ratio'), as well as to the size of banking institutions ('too-big-to-fail'). Each source of risk has now been counterbalanced by increased capital buffers (higher risk weights) or lending and borrowing limits (a leverage ratio) to be fully implemented by 2019.

The regulatory net within the European Union (EU), for instance, has been fundamentally transformed since 2008 in response to the global financial crisis. The European Commission proposed new or reformed directives and regulations that change the modes of financial interaction. Institutions like the European Banking Authority, the European Insurance and Occupational Pension Authority, the European Securities and Markets Authority or the European Systemic Risk Board provide further insights into market operations. Together, these developments impact on a more general conception of financial markets in the EU.

The systemic inter-connectedness of the credit system via shadow banking and across jurisdictions has been enabled by common regulatory constructions and complementary cash flows across the Atlantic. Regulatory agencies, private associations, individual, national and regional actors are all accountable for triggering the build-up of systemic risk and its consequences, although, as separate entities, perhaps unaware of creating an unprotected credit system inherently prone to runs. The systemic disruption of the financial system after the Lehman Brothers' failure highlighted the need for further integration of the international financial order for credit and debt. This paradoxical situation—that is, regulating inter-connectedness via a broader common regulatory framework—may not be resolved without understanding the socio-political underpinnings of the financial system. Further regulation might thus defer but not avoid systemic sensitivity in the times to come.

## 5. Conclusion: Heterodox economics and shadow banking

Shadow banking reflects the increasing homogeneity of the global financial rules that have been pushed in the direction of globally-shared categories for financial regulation and practices. This shift is accompanied by not only an unprecedented compatibility of the varieties of international financial capitalism, but also a synchronicity of reactions and consequences in times of crisis. Thereby, financial regulation becomes part of the production of global categories for risk, resilience and even safety. These aspects, however, are not restricted to the economic domain; nor can they be separated from the sociocultural production of purposes or value systems for financial relations. Heterodox economics, in contrast with the mainstream view, provides several pathways to understand the present regime of accumulation. Heterodox economics not only allows for an abstract analysis of certain value regimes like currencies, government bonds, or other debt securities, but also for an evaluation of the conjunction of financial and societal relations. The orchestration of shadow and traditional banking does not work within clear-cut regulatory (global) space, but shadow banking makes exactly use of the variegation of juridical fields also of matters beyond financial relations. The socio-political aspect of finance and the financial aspect of politics and society have far reaching implications for the reasoning of one value system against another. In this context, finance is one analytical entrance point to understand variegation and its associated socio-political hierarchies.

In this regard, the balance of public and private forces points to an ongoing struggle that is not restricted to the field of finance. The preference for private over public debt, debt over taxes, or growth over sustainability structures the financial world; finance, however, enables specific relations over others when conducted within the social world. This points to a rather old concept in institutional economics, that is, how to value the time to come, expressed in the notion of futurity by John R. Commons at a time when economics had been closer to sociology, history, and other social science disciplines.

The notion of futurity allows for the analysis of conceptions of the future rooted in the present and for the structuring of financial flows. In this way, a broader understanding of the socio-political production for imaginary thinking is needed that considers the institutionalizations of future imaginations in the present. Possibly one of the most prominent accounts may be represented by pension schemes; one of the most popular can be seen in science fiction movies as guidance for technological innovation.

The problem of shadow banking shows the 'plumbing' of such imaginaries, as it directs monetary resources accordingly. The recent global financial crisis and its widespread consequences raised questions not only about economic theory but also about the political system governing global relations. After its seemingly local origin, the market interruption challenged longstanding procedures of central banks, transnational banking, and international financial regulation. The crisis intervened into economic and political procedures previously perceived as the norm for financial interactions. Systemic interruptions, hence, provide a context within which not only the failure of rules comes to light but also the assumptions about the normal perception of a time to come.

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# D – Politics in crisis: Capital requirements as strategies of governance

To highlight the politics of meaning over time, this paper reconstructs the evolution of regulatory texts which were revised or merged and led to the present capital requirements for banks in the European Union. Thus, it shows how distinctive discursive strategies were inscribed into regulation, which in turn arranges the political context. This political context delimits how actorhood can be articulated, what kinds of properties can be attached to it and how different entities relate to each other within European financial regulation. This analysis led to three interrelated narratives. The first starts with the increasing need for jurisdictional alignment between European member states especially between 1972 and 1992. The second proceeds with the insertion of risk into regulatory reasoning between 1992 and 2006. And the third displays the enlarged role for supranational agency vis-à-vis national jurisdictions between 2006 and 2013.

Over time, regulatory texts increasingly used the concept of risk to make sense of the European field of banking regulation. Theoretically, the paper follows Foucault's notion of strategies within *the architecture of knowledge* in showing how discourses situate themselves and thereby open up reconfigured power relations. Methodologically, the paper is based on a thick reading of regulatory text, thereby extracting decisive evolutions and changes in discourse organising concepts, such as member states in their dual role of subjectivities and objects of regulatory measures. This change relates especially to strategies for risk management. All in all, this paper points to the present subordination of democratic decision-making to a management metaphor with the goal to enable a well-functioning market system.

This paper is based on (Wilhelm 2017)

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## 1. Introduction: Strategies in crises

*Madam President, the series of events we have witnessed in financial markets during the last year, and in particular during the last few days, are of a magnitude that exceeds anything we have seen in our lifetime [...] Work is progressing at the Commission, and the Commission will soon come forward with proposals on a revision to the Capital Requirements Directive. (Almunia 2008)*

In his speech to the European Parliament on 24th September 2008, Joaquín Almunia, then European Commissioner for Economic and Monetary Affairs and the Euro, marked the exceptional quality of the recent financial crisis 2008-9. He highlighted how the European Union is going to deal with these exceptional circumstances; namely, by means of further developing the regulatory framework across Europe and by coordinating with other global actors. This rather conventional answer to extraordinary crisis had been made possible over decades. As exceptional the crisis may have been in its depth and reach, the reaction went quite along previously known routines. This paper considers regulatory techniques and mechanisms which made these routines possible in the first place and it asks what kind of political change can be observed behind this rather routine confrontation of crisis over the last 40 or so years. Specifically, this article reconstructs the regulation of capital requirements for banks, i.e. how the so-called CRR/CRD IV package, a main response to the recent financial crisis, came about. The CRR/CRD IV package is concerned with the capital structure of financial institutions and how it affects their strategy to apply leverage through credit provision and investment. In general, regulatory reform demands higher capital buffers for individual financial institutions across the European Union which is meant to make the overall system more stable. This goes hand in hand with defining new investment categories and thereby hierarchies of different investment strategies, for instance, when it comes to investments in mortgage securities in contrast to securities based on car financing schemes.

More recent analyses in International Political Economy about European financial regulation focused on actors and interests and how they were involved in negotiations, commenting and formulating the emerging regulatory setting (Posner and Veron 2010; Tsingou 2010; Mügge 2011; Pagliari and Young 2014; Quaglia 2014). A more structural perspective is concerned with conditions of global governance which may limit possible regulatory proposals (Helleiner 2011; Cohen 2012; Germain 2012; Schwartz 2012). What seems to be rather absent from this discussion, however, is how the articulation of financial regulation constitutes and restricts the dynamic of finance and politics in certain ways (exceptions are Aitken 2010; Hansen and Porter 2012; Langley 2013). Analyses in the latter sense, though less focusing on the matter of financial regulation, were carried out under the umbrella of the Social Studies of Finance (for a similar critique see Riles 2011). They look at what finance does to a social understanding of the world and what the social understanding of finance does to the world (MacKenzie and Millo 2003; Callon 2007; Pryke and du Gay 2007; Armstrong et al. 2012). In this way, such studies are concerned with understandings of technicity (Preda 2006), actor-hood (Hardie and MacKenzie 2007), social practices (Fourcade 2006), the production of knowledge (MacKenzie 2012) or the power of ideas (Baker 2013) to understand how finance is in the making. Against this background, this article proposes that regulatory texts provide a different empirical angel to study the social and political implications of finance. This approach is to look at constitutive processes for and of financial regulation by avoiding the structure/agency divide and, at the same time, by not exclusively focusing on micro-practices of finance either. Hence, using financial regulatory texts as an analytical site enables us to look at the politics of financial regulation as an evolution of distinctive formations, i.e. which types of strategies are resorted to govern the financial system over time.

In Foucault's terms, he refers to 'systems of formation' differentiated via a specific 'regularity of a practice' which he expressed in his earlier work. Following his *Archaeology of knowledge* (Foucault 2002: 71–85) allows to reconstruct distinctive regularities entailing different strategies referring to the, in this case, financial system as an object of governance. Such strategies in a Foucauldian sense express how 'options and thematic choices' are confronted with when they appear. In a specific 'field of stabilization' specific strategies can be repeated and at the same time this field creates the limitations for their expression. It produces a 'threshold beyond which there can be no further equivalence' between strategies and their implied objectives. This is when a new field of stabilisation can be encountered though still 'authorized by anterior levels'. In this sense, the following reconstruction is based on a Foucauldian reading of the regulatory texts that in their revised or merged form have led to the present CRR/CRD IV package in the EU. Hence, the article shows how distinctive formations were inscribed into regulation and how they provide for regulatory strategies which, in turn, arrange a political context to come. Confronted with options and choices, already present sets of strategies condition the way on how actor-hood can be articulated, what kind of properties can be attached to it and how different entities relate to each other, here exemplary within the European financial context but also with implication for governance through standardisation more broadly.

This analysis led to narratives which, as 'field of stabalisation' or 'system of formation', can be arranged as three episodes, each representing a distinctive set of strategies, i.e. how financial interaction on a European scale is reasoned and regulated as well as how they prepare the next steps to come. The narration begins with the increasing need for jurisdictional alignment between European Member States, especially between 1972 and 1992. It continues with the insertion of risk into regulatory reasoning between 1992 and 2006. And it ends with an increased role of supranational agency vis-à-vis national jurisdictions between 2006 and 2013. Over time, the regulatory texts increasingly centre on the concept of risk and its epistemic context to relate to and thus govern the European Union's financial system.[31] In response to recent crisis dynamics and to provide for a stable financial system, the notions of systemic and macro-prudential risks, risk profiles as well as risk management produce a distinctive hierarchy between market actors, Member States and the European Union. This is accompanied by the reconfiguration of the institutional setting of the European Union by creating mechanisms articulated through risk, which are meant to situate its Member States vis-à-vis the needs of functional financial markets. The new regulatory context of risk in financial governance provides a further outlook to a new understanding of state agency as entities to be managed in contrast to self-determined actors as, for example, represented by the former regulatory texts. This, in turn, points to a better understanding of the politics at play along European financial integration and how distinctive regulatory strategies condition how future politics of finance can be articulated. The following first episode highlights the inscription of risk into regulatory texts between the early 1970s and early 1990s and how this stabilised a field for governance within the European Union. An integral part of this was the increased focus on expertise inscribed into strategies of financial governance which in turn develop and prepare for strategies of governance to come.

## 2. The way to risk (1972–1992)

This first episode provides the first context within which the regulation of financial institutions in Europe shows the premise for an alignment of the different Member States. This evolution then leads to the inclusion of risk into regulatory texts. Based on this, risk became part of regulation and the way it

[31] For discussions of the politics of risk more specifically see for instance de Goede 2004; Holzer and Millo 2005; Kessler 2007; Beckert and Berghoff 2013.

required new institutions, calculatory capacities and common standards. This first episode shows the strategies for governance shifting from the coordination of capital flows to the governance of financial institutions from 1973 until 1992. In 1973, the European Community established one of the first agreements 'on the abolition of restrictions on freedom of establishment and freedom to provide services' for the financial sector (EC 1973). It is a ten-page document that is primarily concerned with outlining exceptions for individual countries or country-related specificities of the respective financial sectors. The 1973 directive was meant to enable free capital movement across European jurisdictions whereas, in 1992, the first inclusion of risk into the European governance of financial institutions was adopted (EC 1993a)

The 1973 directive reflected an agreement to interlink different jurisdictions to enable financial interactions across borders. The consequences of these first aspirations already necessitated a certain coordination between Member States and the European level. However, the construction of the subjectivities within this document, as we will see, deviates widely from the present understanding of a Member State of the European Union. Then, it was one article of the regulatory document – i.e. Article 7 – which was responsible for organising potential requirements for cooperation across national boundaries. It prescribed regular meetings to prepare for difficulties related to the regulatory implementation as well as further development to enable desired cooperation.

> The Commission and the representatives of the authorities responsible in the Member States for the supervision of banks and other financial institutions shall meet regularly so that they may facilitate, for the purpose of implementing the Directive, the solution of problems which the authorities might face regarding supervision of the activities covered by this Directive, and shall ensure all appropriate cooperation among themselves within the limits of their respective powers. (EC 1973)

This quote also offers an impression of how Member States were addressed by European regulation four decades ago. For a better understanding of the evolution of the changing contextual meaning of Member States, two more examples might provide an insight into the, by then, normal notion of membership. Firstly, the entities addressed in this legislative act are financial institutions and their ability to situate themselves within different jurisdictions. The objects of concern are 'the natural persons and companies or firms' which is in stark contrast to previous considerations around 'the widest and most speedy liberalisation of capital movements' (EC 1960). Secondly and already in 1963, the notion of transactions between Member States was complemented by the notion of services to 'ensure the satisfactory establishment and functioning of a common market' (EC 1963) which then led to the regulation of 'banks and other financial institutions' in 1973.

Both instances show how the governance coordination between Member States produces shared categories of financial institutions and practices and, therefore, a common understanding of regulatory objects of concern. Five years on, in 1977, the way in which Member States connect to each other was refined along the problems of free capital movements, provision of information by financial institutions as well as coordinated supervisory structures. In this regard, the following quote highlights three regulatory techniques applied at that time, i.e. 'closely', 'all' as well as 'likely'. Each expression renders it necessary to specify the structure of cooperation and the differentiation as well as the quality of information.

> The competent authorities of the Member States concerned shall collaborate *closely* in order to supervise the activities of credit institutions operating, in particular by having established branches there, in one or more Member State other than that in which their head offices are situated. They shall supply one another with *all* information concerning the management and ownership of such credit institutions that is *likely* to facilitate their supervision and the examination of the conditions for their authorisation and all information *likely* to facilitate the monitoring of their liquidity and solvency. (EC 1977, my highlights)

In contrast to prior versions of the regulatory setting, the need to exchange information in very specific ways comes up as the main concern. In this case, it means that there is not only an increased flow of information between the supervisory institutions, but also, that certain standards are to be established to create the conditions for a reciprocal and homogenous exchange of information. Information regarding management and ownership had to be categorised, adopted and translated beyond the then present jurisdictional confines. Member States are considered as having a common and reciprocal obligation, i.e. at this stage, to specify at least 'certain minimum requirements to be imposed by all Member States' (EC 1977). Member states are no longer restricted to their individual differences; they also have common obligations to deal with credit institutions. A newly established common forum further displays this regulatory evolution. This so-called 'Advisory Committee' was not only a specific forum where Member States' as well as Commission representatives could come together, it also constructed the preconditions needed to include expert knowledge in the consultation process leading to financial regulation and supervisory structures, as the committee ‘may be accompanied by advisers from time and subject to the prior agreement’ (EC 1977).[32]

When the forum was asked to provide information on the supranational level, Member States could be confronted with this information. Such a reconfiguration of positions of Member States and of the European level points to some strategies used to relate state agency with need for information and expertise as well as the resulting institutional setting. This, in turn, allows to demark a more general field of stabilisation. Knowledge production could be used as a strategy to relate and assimilate national, legal, economic or bureaucratic routines. Prior to this development, Member States could provide expertise through their national bureaucracies and confront each other with this ‘unilateral’ knowledge. Their regulatory needs were based on distinct processes of knowledge production. Though transnational, financial markets could be regarded as free of a pre-defined European institutional prism through which pre-specified categories select and hierarchize the information needed.

Later, in 1983, a directive was brought under way, explicitly providing a common supervisory structure, i.e. that ‘controls and supervisory practices applicable to credit institutions operating within the Community must be broadly similar from one Member State to another’ (EC 1983). Minimum standards in all Member States were meant to ‘eliminate the most obstructive differences between the laws of the Member States’ (EC 1983). Thus, this directive predominantly focused on the legal structure of the Member States which had to be aligned according to the conditions set by the transnational financial system and promoted beforehand. This supervision under a consolidated basis formulates the shared duties of supervisory agencies in different countries to make information about financial institutions reciprocally accessible.[33] The remarkable shift of the 1983 setting, in contrast to its complementing 1992 directive, was that the latter for the first time specified an understanding of risk. Indeed, reading the following quote, the use of risk seems to be twofold: On the one hand, risk is associated with the market in general, i.e. ‘market risks’; on the other hand, there is a reference to the particular nature of risks, i.e. an understanding of risk which can be differentiated along its potential to affect financial institutions within a market. What is also indicated is how risks can be approached, namely through ‘methods determined by those authorities in the light of the particular nature of the risks

[32] Later-on, this development was further institutionalised by the Lamfalussy procedure.

[33] Not discussed at this point are the directives concerning balance sheet layout (EC 1986) and the monitoring and controlling of large exposures (EC 1987). Both directives are interesting places to find early minimum harmonisation of different jurisdictional traditions regarding, on the one hand, accounting rules for different financial products and, on the other hand, the discussion on what kind of leverage ratios as well as their differentiation are seen to be acceptable.

involved' (EC 1992). This, in turn, highlights the technical context (as a field of stabilisation) which had been prepared beforehand and within which the notion of risk could then be placed via changing strategies for governance.

By articulating risk, this directive allows to differentiate the field to be covered. The Directive allows to represent market mechanisms as something that is outside of the Directive and it implies different categories of risks to be considered. Risk is able to generate the entities to be governed and, at the same time, it stabilises an overreaching field for knowledge formation regarding these entities. Risk is, thus, formulated as something independent of the regulatory matters. The risk setting can be classed by the 'nature' of risk and it provides the basis for the decision on which kinds of risks do affect financial institutions and which kinds of risks do not.[34] What is not yet laid out is the form of 'regulation as risk' in terms of presupposed understandings of how risk is to be handled by regulated entities.

Looking at the European regulation of financial institutions, this first period between 1972 and 1992 provides the basic parameters of transnational capital movements. Financial regulation in this regard allowed for an alignment of different national jurisdictions, through multinational coordination, by specifying entities, products as well as information procedures and, to supervise these activities, new institutions and entrance points for expertise had been created. This first episode, outlined above, ends with the first inscription of risk within European financial regulation, which can be understood as a strategy to control and supervise transnational practices of financial institutions.

## 3. From risk to management (1993–2006)

The first episode ended in 1992 by stating that new tools, institutions and categories had been developed to supervise financial institutions in a transnational market. In the aftermath, and here this second episode starts, the notion of capital adequacy was introduced through the so-called Capital Adequacy Directive (CAD) in 1993 (EC 1993b). The differentiation of risk, discussed above, opened-up the notion of market risks and allowed for the insertion of further risk categories, e.g. counter-party risk, foreign-exchange risk, risk of loss, risk of price change, position risk and many others (EC 1993b). Thereby, this episode shows how the field of stabilization changed and further evolved the leading determinants in organising financial governance. Whereas the first

[34] The notion of risk referred to in Council Directive 92/121/EEC focuses on acceptable hedging strategies (EC 1993). It therefore provides a basis for a discussion on the processes structuring the market within the European Union along static prescripts for hedging practices.

episode highlighted the need for alignment of different jurisdictions through a shared understanding of financial institutions and practices, this second episode concentrates on the increased use of the notion of risk in its multifaceted form.

This shift allowed governance to turn to an abstraction of financial entities and practices as they had been categorised through risk calculation. This, in turn, allowed for a management of finance through regulation in the sense that it could be governed by an adjustment of numbers (i.e. of capital adequacy), based on the alignment of categories across jurisdictions. Due to the CAD measures mentioned above, capital adequacy was not only a tool to increase the mutual recognition of financial institutions by the different Member States, it was also the starting point to find a common logic of financial governance, even though, at this point in time, the directive explicitly states that it does neither 'establish common standards' nor 'establish the amounts of the initial capital'. It solely concentrates on the 'essential harmonization that is necessary and sufficient to secure the mutual recognition of authorization and of prudential supervision systems' (EC 1993b).

This second episode revolves around the year 2000 when most of the directives mentioned so far were combined under one legislation. This consolidation, however, did not mean that the regulatory environment stayed the same (the new directive being only the sum of its former parts). The directive 'relating to the taking up and pursuit of the business of credit institutions' (EC 2000) was, especially compared to the previous documents, highly technical, detailed and presented a rich description of financial practices and how they relate to each other. In 2000, the arguments for common regulation highlighted the need for homogeneity as 'credit institutions are engaged in direct competition with one another and monitoring requirements throughout the Community should therefore be equivalent.' (EC 2000)

In a first step, regulation is no longer seen as an enabling force that allows for transnational capital flows. Quite to the contrary, regulatory variation is now seen as a hindrance to fair competition. Secondly and based on the condition of direct competition between financial institutions across Europe, the governance structure does not only have to be aligned but regulatory homogeneity also generates the increasing importance of the European policy making level. By positioning the Community as the level of measurement for fair competition, the regulatory discourse of financial standards can only be meaningfully situated at the very same level. The governance throughout the Community as well as the specific regulatory field are thereby interlinked and jurisdictional differences are solved using the new hierarchy of governance. This means that it is now the structure of the markets which renders it necessary to change the regulation in contrast to a political interest to create a common market across borders. The text continues: 'To that end, the criteria applied to determining the concentration of exposures must be the subject of legally binding rules at Community level and cannot be left entirely to the discretion of the Member States.' (EC 2000)

Member States are considered as only partially in charge of legislative procedures. The functioning of the market within a legislative context is no longer in accordance with the prerogative potential of the Member States. The level playing field (for fair competition as well as the strengthening of the internal banking system) provides the field of stabilisation for the argument to place the Community's interest above that of the individual Member States. To establish control over the common market, the notion of risk is further developed within the regulatory text. Using this notion, regulation allows to specify the set-up of financial institutions and financial practices via measurements connective to risk categories.

For instance, using risk weightings, a different kind of strategy to govern finance becomes central. Before, the supervisory agencies within Member States had their prerogative in assessing different institutions and their exposure to credit or other risks. Matters to be defined on the European level then focused on practices indicating the workings of information exchange and the different forms and levels of cooperation between national agencies and other, nationally rooted, supervisory agencies. Now in contrast, the incentives to structure the capital within banks is governed on the European level using an adjustment of numbers as risk weightings – the logic of control is thus not to monitor different institutions in the same way but to establish a common field for capital hierarchies. The field of stabilisation now concerns financial products and their properties when assembled on banks' balance sheets whereas before it was about the trading entities.

Based on the structure provided by different registers of risk, supervisors are now able to evaluate the financial institutions based on their risk weighted capital structure and to provide minimum capital requirements for financial institutions. Financial institutions, in turn, can then be evaluated on a daily basis using the 'mark to market' value of their capital provisions and hence their varying leverage ratios. The 2006 directives (EU 2006a; 2006b) therefore not only institute capital requirements as a representation for further inscription of risk into financial regulation, they also provide for an expansion of supervisory techniques able to harmonise different Member States' provisions and to reach beyond the nationally confined supervisory techniques and instruments.

> Minimum capital requirements play a central role in the supervision of credit institutions and in the mutual recognition of supervisory techniques. In that respect, the provisions on minimum capital requirements should be considered in conjunction with other specific

> instruments also harmonising the fundamental techniques for the supervision of credit institutions. (EU 2006a)

Taken together, common capital requirements derive from the distinctive contingency which relates to the free movement of capital, a distinctive notion of risk, and institutional abilities of control. A common scheme for capital requirements then 'prevent distortions of competition', they 'strengthen the banking system' and ensure 'adequate solvency'. '[D]ifferent levels of risk-sensitivity' allow addressing very different forms of financial institutions. This expansion is made possible by new techniques applied in finance 'as external ratings and credit institutions' own estimates of individual credit risk parameters represents a significant enhancement in the risk-sensitivity and prudential soundness of the credit risk rules'. (EU 2006a)

In this context, especially the notion of 'risk-sensitivity' stands out for understanding how the financial system is in the making. The emergence of the notion of risk-sensitivity indicates that financial markets cannot provide an adequate valuation of financial products, as risk can be calculated independently from prices through risk models or external ratings. Considering the at that time ever increasing practices of over-the-counter deals, this means that ratings and models attached to certain categories of financial products create a quasi-market not concerned with valuation and prices but with evaluation and risk. Such a market is then able to provide information about categorical risks (e.g. for RMBSs) instead of prices (e.g. for Facebook shares). In this respect, the notion of risk-sensitivity relates to systemic control of financial interactions via its ability to establish categorical entrance points regarding financial flows.

This new conceptual constellation changes the focal point of regulation away from concrete requirements and turns it to a broader reference i.e. the structure of markets and how to treat them properly. The revised rules for financial institutions based on risk-sensitivity open-up the space for a management of the markets in contrast to regulating market participants or Member States' interactions, that is if 'minimum capital requirements […] have significant effects on the economic cycle' (EU 2006a). The object to be regulated then becomes more of a 'conduct of conduct'[35] as opposed to a reference to concrete interactions between market participants. The capital requirements/risk conjunction appears here as a central mechanism for controlling the financial field in contrast to controlling the financial agents active within. The notion of risk thereby enables systemic references (e.g. to connect to the economic cycle) as a more general indicator of economic performance and

[35] A 'conduct of conduct' is the Foucauldian understanding of government as 'a form of activity aiming to shape, guide or affect the conduct of some person or persons'. (Gordon, 1991: 2)

thus the management of the economic context for financial institutions. This implies that the prerogative to govern the financial field goes hand in hand with a reduced relevance of the individual financial institution.

Such a strategy entails that, when the playing field is controlled in the right way, the players are able to compete independently by realising the pre-determined scope of possible financial activities.[36] Such a rationale can even be connected to a more global perspective on the functioning of financial markets, as it was the internationally relevant Basel II agreement by the Basel Committee for Banking Supervision which had been the predecessor of the recently established CRR/CRD IV package (EU 2013a; 2013b). The third episode continues by showing how the enabling conditions for the management of the financial field presented above expands to include not only financial but also political institutions, namely the institutional structure of the EU's Member States. Below, this will be further illustrated along the continued evolution of the rules for capital requirements along the recent crisis experience.

## 4. From markets to states (2006–2013)

The second episode already indicated how the strategic changes from a governance of financial institutions to a governance of markets affected the regulatory description of Member States and the Community and thereby their position within financial regulation as the broader field of stabilisation. Member States are no longer at the centre of concern; they are now part of the complex constellation of financial markets. This third episode suggests, that they are to be streamlined to allow for an effective running of the EU's internal banking market. To understand this evolution, third episode considers the revision of capital adequacy requirements concerned with 'the convergence of supervisory practices throughout the Community' (EU 2006b). Whereas before it was an explicit call against an overreaching harmonisation and a rejection of the Community's involvement into the standards of national supervision, it is now the regulatory goal to assimilate the different supervisory practices. The key aspects of this are prudential measures evolving in the post crisis context.

The insertion of expertise and the new role of community level financial governance developed in the prior episodes, converged into a regular ex-

[36] This is in line with the discussion on the different juridical forms of regulatory harmonisation (e.g. concerning European capital markets) and regulatory competition (e.g. in European company law), for a discussion see Zumbansen 2006 and Schammo 2011.

change between supervisory agencies as for instance the Committee of European Banking Supervisors 'should report on a yearly basis to the Community Institutions on progress made' (EU 2006b). Indeed, the direction of such regulatory matters had already been established in the pretext for further implementation of supervisory practices. It was the then financial crisis which triggered a request by the Commission in 2009 explicating the need to establish four additional institutions on the supranational level to create mechanisms for supervision.[37] Mechanisms and techniques already known could be put in place to adapt to the exceptional circumstances provided by the crisis' dynamics. This was undertaken not only to confront the by then present crisis but also to prevent future disruptions. In 2012, the high-level group around Jacques de Larosière 'concluded that the supervisory framework of the financial sector of the Union needed to be strengthened to reduce the risk and severity of future financial crises and recommended far-reaching reforms to the structure of supervision of that sector' (EU 2012).

These far-reaching reforms and the new institutional setting led to new strategies through which financial markets could be addressed by regulation. On the one hand, the European Union now considers not only internal differences of regulation and their consequences for further regulation but also how internal reforms affect the relation to other regulatory jurisdictions (i.e. third countries). On the other hand, the institutional setting now allows addressing specific financial products and their trading practices at the European level. There, concrete supervision is no longer left to the national level. An increasing pursuit of over-the-counter practices across national jurisdiction and lacking EU-wide regulatory efforts necessitate supranational coordination of European rules by further explicating how these practices are to be undertaken. This evolution leads to the most recent rules for capital requirements, which are based on a directive as well as on a regulation on capital requirements (short CRD and CRR respectively).

This changing strategy implies a basic difference to prior documents, as the regulation is to be directly translated into national law without the range for manoeuvring provided in contrast by a directive.[38] Hence, categories within European financial regulation in this field are transmitted more directly into national law. The need for risk calculations related to these practices establishes the connection to the contextual regulatory framework beyond the banking sector or specific capital requirements. Here, the predominant prac-

[37] The European Banking Authority (EBA), European Systemic Risk Board (ESRB), European Insurance and European Insurance and Occupational Pensions Authority (EIOPA) and European Security and Markets Authority (ESMA)

[38] For an extensive discussion about the consequences of the two regulatory techniques regarding finance see Howarth and Quaglia (2013).

tices for trading between financial institutions create a framework for European regulation. Concrete financial practices are increasingly inscribed into regulation which basically means moving away from politics based on state interests as it might had been the case before (see the first episode above) but to pursue regulatory needs along technical fixes provided and demanded by the financial field. Hence, financial regulation itself represents how concepts of finance (and thereby also of politics) are to be realised.

This can especially be illustrated when looking at how the changing field of stabilisation allowed for different means to address 'Member States' via financial regulation. The point that stands out here is not only (as already described) the changing configuration of financial markets through the articulation of risk, but now the way how the former agencies for making financial regulation are now seen as one of its means. The basic difference to the 1972 documents is that the Member States were the main actors able to set the term of negotiation for international exchange. In contrast, after 2000 it is no longer about relating the differences between Member States but about the common and harmonised regulatory system which should be developed further. Oversight and supervision then is a European prerogative – Member States are simply meant to comply. The measures regarding upgrading and strengthening supervision point to the featured position of the community level in contrast to an undermined Member State' prerogative.

Beyond the position of Member States so indicated, it is also about how financial knowledge and standards should be changed independently of national jurisdictions and related variations. It is not only the need for harmonisation but also the tools to do so that are framed in a universalist way. Financial markets are to be provided with a level playing field which also means having common standards and a common supervisory agency (or network of agencies). On the European level, this reasoning enables supervisory agencies to report on Member States. For regulation, it is now possible to address Member States as objects of regulatory needs. Here, the CRR/CRD IV framework is just one example of how Member States are subject to supervisory processes due to stabilisation or transparency needs set out and required on the European level.

> Having regard to work of the BCBS' Standards Implementation Group in monitoring and reviewing member countries' implementation of the Basel III framework, the Commission should provide update reports on an ongoing basis, and at least following the publication of each Progress Report by BCBS, on the implementation and domestic adoption of the Basel III framework in other major jurisdictions, including an assessment of the consistency of other countries' legislation or regulations with the international minimum standards, in order to identify differences that could raise level playing field concerns. (EU 2013a)

The quote shows how Member States are situated in a new governance structure to build up routines of which they are part of. Reviews and assessments are directed to the Member States whereas the community level is in the position to decide what is of concern along the inter-jurisdictional presumption of homogeneity, i.e. along the need for a level playing field. This revised hierarchical relation functions by a different set of strategies than what could be observed in the previous episodes. Now, the level playing field notion considers internal market categories which were promoted by the regulatory evolution. This means that, whereas previously regulation was produced along enabling conditions (transnational capital flows, fair competition), it is now reasoned along a market perspective only created beforehand. The financial market understanding of what is meant to be a level playing field is now taken as a basis of what can be discussed to be effective financial regulation. This confined field of stabilization at the conjunction of finance and financial regulation, in turn, restricts the regulatory position of Member States and broader formations of interest.

Beginning in 2000, initial expressions like 'Member States should be allowed to' (EC 2000) or 'Member States should be encouraged', 'Member States should be able to', (EU 2004) give another impression of how a superior order is presumed to be able to affect Member States' actions. A pre-set regulatory environment is constituted within which action is to a higher or lesser degree incentivised measured determined along the regulatory framework itself. This stands in contrast to a discussion about what the actual purpose of the 'thing' to be regulated might be for other fields. Potential actions are thereby already presumed by the contingent evolution of financial regulation displayed above. In this way, the regulatory strategy reconstructed in this section indicates how regulation moved from addressing markets to managing states which in turn become from strategical point of view inferior to the regulatory framework in place. The notion of risk enabled categories to articulate markets as existing social formations. The market sphere thereby established rendered it necessary to demand further consistencies by further addressing the regulatory structure within Member States in order to put up a consistent level playing field at the European level.

## 5. Conclusion: Politics in crisis

In this paper, I showed three sets of strategies which allow for different possibilities of governance via financial regulation. The central mechanism used to do so surrounds the concept of risk and the discursive position of agencies, objects or strategies related to the notion of Member States. The new dynamics along the financial crisis 2008-9 created new relations between regulatory bodies, financial institutions, governments and parliaments at the European as well as at the national level. Hence, European regulation alters the meaning and possibilities of Member States and thus the representation of state sovereignty. The overall development of financial regulation represents the changing fields of stabilization, how they entail different strategies and how this allows for or hinders political intervention, i.e. how each episode represents a distinctive set of strategies, which are used to render things governable.

The present regulatory context of risk in financial governance gives a further outlook on a new understanding of state agencies as entities to be managed in contrast to self-determined actors, as for example, represented within the former regulatory texts of the early 1970s. Looking at this evolution allows for a better understanding of the present formation and role of the European Union. Within this discourse, it is up to the states which found themselves in this situation to re-calibrate their financial position vis-á-vis financial institutions. Capital requirements, in this case, allow for a specific standard able to intervene from afar on the very immediate level of individual financial institutions and their balance sheets. At the same time, the level on which the information is gathered goes beyond the states' (traditional) agency, i.e. financial regulation requires Member States to adjust to the categories of supervision.

Now there are two pathways. What this article indeed does not want is to argue for a break-up of the European Union to allow states to regain 'their' sovereignty. Quite to the contrary, the politics of self-interest may rather be a major driving force along which the marketization of the European Union could be facilitated especially via avoiding constructing a political union in addition to the commercial union. What can be distilled from this article is thus when to market logic will proceed to be the guiding rational for organizing social relations disintegration with the widely discussed adverse effects might be the nearest consequence.

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# E – Reflexivity of shadow banking

The reflexive relations of finance and regulation point to the importance of shadow banking and its significance for global financial hierarchies. Pierre Bourdieu, discussing the production of the economic field, accentuated the power struggles involved when it comes to processes of (economic) integration. Thus, this paper highlights the role of shadow banking and its regulation for integrating the global financial field. Following Bourdieu, the paper argues that the homogenisation of the standard setting discourse, i.e. international financial regulation, after the recent financial crisis, further concentrates the resources for domination on a global scale via the reflexive processes of finance and its regulation, visible via the problem of shadow banking.

The paper proceeds in two parts. First, it positions reflexivity on the field level and points to the central position of shadow banking for further homogenisation within finance. Second, the article provides a more granular reconstruction of the present regulatory discussion regarding the reflexivity of shadow banking as a central node for the further integration of the global financial field. The article concludes with the political and social implications of recent financial governance, i.e. the increasing dominance of an 'economistic' as against a political-democratic rationale. Subsequently, also the shadow banking comes to rely on a fragile and hidden framework for financial exchange generating profits in the present and deferring possible systemic failure, and hence widespread losses, into a precarious future.

Thus, the further evolution of shadow banking provides a wide opening for research into the reflexive interaction of financial innovation and regulation, not as separate forces but as an intersection that indicates how financial markets express contemporary hierarchies of domination, apart from democratic decision-making. The article thus clarifies the socio-political location for international (shadow) banking.

This paper is based on (Wilhelm 2017).

Wilhelm, B. 2017. 'Reflexivity of Shadow Banking', in *The Routledge Companion to Banking Regulation and Reform*, Ertürk, I. & Gabor, D. (eds), Abingdon: Routledge, pp. 74–83.

# 1. Introduction

Reflexive relations of finance and regulation point to the importance of shadow banking and its role for global financial hierarchies. Pierre Bourdieu discussing the production of the economic field accentuated the power struggle involved when it comes to processes of (economic) integration. Thus, this article highlights the role of shadow banking and its regulation for integrating the global financial field. Following Bourdieu, it argues that the homogenisation of the standard setting discourse, i.e. international financial regulation, after the recent financial crisis further concentrates the resources for domination on a global scale via the reflexive process of finance and its regulation along the problem of shadow banking.

Shadow banking is understood as a focal point for the performance of finance and its regulation. The chapter shows how these two fields interact and, indeed, how they constitute each other. The co-constitutive forces shape and make (shadow) banking, its bubbles, crises and they perpetuate dominance in the present, increasingly integrated 'global economic field' (Bourdieu, 2005). Globally shared standards and therefore an integrated financial and economic system provide for a synchronic experience of financial practices and crises (Nesvetailova, 2014; Kalemli-Ozcan, Papaioannou and Peydro, 2013; Frankel and Rose, 1998). Standards for such integration, however, put further emphasis on regulators as co-drivers for the perpetuation of dominance throughout the financial field.

The so-called run on the shadow banking system in 2008 had been followed by a reform agenda which is now at the point to integrate shadow banking practices into international regulatory frameworks, in particular via 'simple, transparent and standardised (STS) securitisation' (EC, 2015; BCBS and IOSCO, 2015). Whereas the Financial Stability Board (FSB) and others support 'non-bank credit intermediation' as it 'provides a valuable alternative to bank funding which supports real economic activity' (FSB, 2014b), it is still open for discussion what this actually means for the financial field and for relations of political dominance therein and beyond.

The chapter proceeds in two steps. First, it positions reflexivity on a field level and points to the central position of shadow banking for further homogenisation in finance. Second, the chapter provides a more granular reconstruction of the present regulatory discussion regarding the reflexivity of shadow banking which marks a central node for the further integration of the global financial field. The chapter concludes then with the central political and social implications of recent financial governance, i.e. an increasing dominance of an 'economistic' against a political-democratic rational.

## 2. Politics of reflexivity

The use of reflexivity in social science broadly understood relates to the subject/object distinction and to their co-constitutive performance often applied to the researcher and her reflexive relation with the (social) world she studies (Hamati-Ataya, 2013; Leander, 2002; Lynch, 2000; Woolgar, 1988). Here, Pierre Bourdieu fosters the self-awareness of the sociologist in analysing the sociality around her. Reflexivity in this way seems to be bound to individual (human) capacities to see the world and their part in the making of the (social) world. In economic sociology, such an anthropological style of research contributed to a better understanding of practices and conditions of social exchange within the financial field (e.g. Zaloom, 2006; Riles, 2011; Abolafia, 1996).

Complementary, this section highlights a further style of reasoning when it comes to reflexive relations, i.e. to observe how homogenisation of the financial field has spread after the post-crisis reform agenda through the relation between financial practices and financial regulation. Not just in times of crisis, researchers may question their own stand to describe a reality not yet in place. However, an experience of crisis usually interferes with a taken for granted logic of how 'things' happen and such an experience therefore calls for more foundational adjustments. These may happen through a basic reconfiguration of categories within a theory in order to adapt to new series of events and hence to change the normal behaviour of doing research.

### 2.1 Reflexivity and its subject

A reflexive understanding problematises standard positivist assumptions like objectification, generalisation or causation. Events of crises indeed may question the very definition of what such categories may refer to. Such events might question theoretical and methodological underpinnings (as well as delineation) of disciplines. Reflexivity in this sense is not only bound to the relation of a researcher and her object but also related to the performance of a social context which makes her a researcher, for instance a sociologist, and her object an object of study, for instance, perceived as being a (or in) crisis. Object and subject gain their specific role thereby not from an outer (empirical or scientific) world but through a specific compatibility of (or conflict within) social fields (Bourdieu, 1985). Events are thus not already present but are continuously constituted via compatible references regarding their presence.

The event of a financial crisis is thereby made obvious through how different observations relate to each other. For the present crisis two forms of observation seem indicative to understand its roots, consequences and how it is to be overcome: innovations in financial practices and their regulation. Both aspects share a considerable focus on the 'problem' of shadow banking. Indeed, the notion of shadow banking itself is a by-product of a crisis experience represented in a recent and widely shared regulatory discourse. Such reflexive perspectives on the discursive conditions of crisis and finance had rather not been centre stage (for an indicative exception see Dorn, 2011).

Understandably, a probably larger social fraction demanded for ways to compensate their losses or increase their profits within and after the financial turmoil. An investor's opinion on reflexivity might have been more useful than the one of a passed away sociologist. What Bourdieu, and indeed already quite a while ago, argued however was that an increasing homogenisation of economic fields in the context of fast information technology goes along with the perpetuation and strengthening of relations of dominance already present: 'We know that, as a general rule, formal equality in a situation of real inequality favours the dominant' (Bourdieu, 2005, p. 225).

Frequently, the notion of reflexivity seems to be reserved for the interaction of the researcher with her field. In contrast to this perception, more systemic approaches à la Parson or Luhmann account for the interactions of different fields (to stay with the Bourdieusian parlance) that contain and produce research subjectivities and their objects. The observation of such a reflexive interplay brings to light how second order observations (now to stick with a Luhmannian grammar) constitute and indeed are able to perform each other.

The regulatory discussion concerning shadow banking serves as an exemplar to show how the reflexive relation of the regulatory discourse interacts with the practice of banking and how this interaction performs systemic (in)stability. Whereas broader (economic) discussions understand this as a kind of feedback loop of regulation and innovation (sometimes referred to as 'reflexive governance,' Voß, Bauknecht and Kemp, 2006), the point being made here is that the present state of the international financial architecture hardly allows for the distinction between the 'fields' of practice and prescription and thus for the assumption of pre-set entities (be it institutions or events) triggering each other.

Positivist approaches try to overcome this problematique of resemblance through an extension of 'surveillance' capacities, thereby gaining a higher degree of granularity regarding the field and thus being able to frame hypotheses accordingly (Fligstein and McAdam, 2012, p. 188). Consequently, a problem of explanation points to a problem of data availability and thereby forgetting about methodologically and theoretically rooted limitations of perspective. The constitutive practice of information computing however already and reflexively pre-sets the range of possible understandings in accordance with methodological/theoretical needs for explanation and surveillance techniques set in place. Thus, data generation is closely related to the structure of dominant modes of research that, in turn, points to the reflexive politics of an object/subject distinction.

In the case of financial regulation and financial practices respectively, the empirical fixation of the problem of shadow banking associated with data generation, the need for transparency, standardisation and complexity reduction, as useful as such enterprises may be, rather points to the already present structure of dominance which may hardly be separated from the form of knowledge production. The reflexivity of the financial field can thereby be traced along the making of the financial architecture concerning the 'problem' of shadow banking briefly outlined below.

### 2.2 Reflexive financial architecture

The new financial architecture after the crisis – and thus the practice of shadow banking – points to the plea for an economic sociology of law in resent years (Ashiagbor, Kotiswaran and Perry-Kessaris, 2013; Swedberg, 2003), as the transnational legal structure of finance highlights the convergence of different disciplinary perspectives. Indeed, what has already and often been shown is how the distinction of an economic, political, legal or social sphere rather resembles a modernist/positivist ideology of clear-cut categories to be found 'out there'. This is further accentuated via the performativity literature, which provides one entrance point to counter such macro causation short cuts via a focus on how (financial) things unfold (Callon, 2010; Aspers, 2007; MacKenzie, 2003). In this way, the 'problem' of shadow banking indicates the construction of certain perspectival categories and hence how such categories and their relations very much depend on reflexive relations.

International exchanges are not immediately visible on the banks' balance sheets though they are backed by shared legal understandings be it for appropriate collateral, haircuts or price-formations more generally. In this way, shadow banking provides a contemporary representation of how the global economic field is sustained and enlarged through rapid financial flows seemingly disconnected from national jurisdictions or other social formations. In contrast to a sovereign prerogative to contain markets, financial engineering not only synchronises financial categories like capital, profitability or the scope for transactions but this practice also functions as a constitutive driver for transnational harmonisation of financial standards.

Even though practices of shadow banking enable to circumvent balance sheet restrictions, these practices are adaptive to international capital flows increasingly defined via international financial rules. Capital requirements in this respect are a central node to understand this evolution as they define the profitability of the bright as well as the gravity of the shady side of finance. This shared horizon for (shadow) banking activities defines and differentiates the notion of capital on a global scale and increasingly harmonises the strategies also for shadow banking activities. Indeed, the present regulatory agenda along the Basel III reforms put further emphasis on responsive capital standards based on respective financial or economic conditions. Legal, financial or economic rationales are thereby intertwined and create the space for shadow banking practices.

The problem of shadow banking for financial stability triggers a more responsive regulatory framework especially regarding the structure of banks' balance sheets. This concerns, on the one hand, more transparent 'look through' capacities for regulators in order to see how banks relate to the shadow banking system via special purpose vehicles or the like (as a micro perspective); and, on the other hand, the new regulatory environment points to an automatic adaptation to more general economic conditions, for instance related to investment regions (bringing in a macro-prudential regulatory perspective). Both aspects further increase the reciprocity of different legal, financial and economic fields and provide for a deeper integration of global financial exchange.

Leading indicators such as GDP growth, main calculatory practices regarding risk or an inbuilt feedback loop to increase the sensitivity of regulatory practices point to the mechanistic understanding of a closely interconnected financial machinery. Thereby, the political role of regulatory institutions or, more broadly, the reflexivity of social relations and financial exchanges are hidden behind a functional logic that excludes a more contested perspective besides efficiency, transparency or data mining. In the following section, tow aspects (risk calculation and intermediation chains) of present financial practice are exemplary to show how harmonisation is enhanced via the reference to the shadow banking system and by leaving peripheral alternatives aside.

## 3. Reflexivity of shadow banking

Confronted with the global implications of shadow banking contraction, the G20 put up a regulatory agenda focusing on stabilising the financial system and thereby also the shadow banking sector. Even though the notion of shadow banking created a new epistemic basin for the present financial system as it brought together legal, economic and also political discussions regarding modern finance – its indicated fallacies had already been discussed some time before. The implications of complex securitisation (Plantin, 2011), the use of special purpose vehicles (Gorton and Souleles, 2005), problems of off balance sheet activities (BCBS, 1986) or the problem of systemic risk (Hellwig, 1995) and the need of macro-prudential regulation (Borio, 2005) had been on the table already before the notion of shadow banking came up though it further aligned these debates (FSB, 2013).

Considering that the shadow banking system generates 'benefits for the financial system and real economy, for example by providing alternative financing to the economy and by creating competition in financial markets that may lead to innovation, efficient credit allocation and cost reduction' (FSB, 2014b), ex post regulatory proposals can also be read as a blue print to normalise such intermediation chains and risk mitigation strategies. The different Basel frameworks for banking regulation connected the international banking system more closely by providing common standards especially for capital and capital transactions. Thereby, securitisation could be pursued within an internationalised market and via a common understanding of risk leading to financial exchanges decreasingly hindered through jurisdictional diversity.

Most recently, the problem of shadow banking provided for a focus on responsive instruments of international financial regulation. Regulatory standards for capital should be related to contextual conditions and they should account for new information about present and future developments of markets. These changes in turn affect the solidity of the capital basis of banking institutions. Such a new paradigm for regulatory standards sets the stage for a marketisation of regulatory adjustments. Shadow banking thus provides a central link for financial and 'regulatory markets'. Two discursive nodes are discussed below as they exemplarily show how, first, off-balance sheet activities produce and sustain (shadow) banking and, secondly, how balance sheets are managed via calculatory practices of risk.

### 3.1 Off-balance credit intermediation

The sensitivity of financial regulation increased compared to the Basel I framework. Financial innovations structure asset portfolios in order to benefit from the more complex risk hierarchies implemented via Basel II. However, what appears in the first place as a success of the regulatory process turns out to trigger demand in tailored investment products off the banks' balance sheets. Shadow banking could produce such products and gained importance for (global) financial intermediation (Plantin, 2014). Or as the Joint Forum states: '[b]ecause the Basel II framework is more risk sensitive, it is likely to have a material effect on bank investors in terms of their interest in various types of securities' (Joint Forum, 2009, p. 18).

Such reflexive dynamisms display how the problem of shadow banking sustains the regulatory discourse with regard to the notion of risk. First, it positions the term as a central node for regulatory organisation and second it inscribes its implication into daily regulatory and bank governance. A further perspective points to how the transmission of credit through chains for intermediation further shifts the power from regulatory to bank governance, whereby the problem of shadow banking provides a catalyser for the enlarged authority of financial rationales in contrast to societal functions such as credit provision, financial stability or social security.

Most comprehensively, shadow banking is defined as non-bank intermediation (FSB, 2011). This points to the critical moment after the Lehman failure in 2008 triggering a run on the shadow banking system. What seemingly made traditional bank runs old fashioned did not apply for modern shadow banking as for this sector there was no deposit insurance scheme in place or an intervention routine by central banks. Hence, the collapse of the shadow banking sector and its opaque interconnectedness to the traditional banking sector is still a main target of the regulatory agenda (IMF, 2014; FSB, 2014a).

What was and still is needed to manufacture money-like securities is a high degree of standardisation, i.e. a high degree of information insensitivity pared with broadly accepted standards for transparency. Both had been delivered through the standardisation of asset classes (like securities backed by prime mortgages) and external ratings provided by credit rating agencies. Together these aspects define the regulatory capital needed in order to back up investments into such products. This combination created an 'opaque' and at the same time clear investment incentive in favour of asset backed securities and securities thereof (Gorton, 2015).

The expansion of the shadow banking system reflected a shared feeling of having enough information about abstract categories like a senior tranche of a mortgage portfolio. Further, risk calculations regarding the construction of the structured investment products made them appear to be immune to detailed disclosures of the performance of individual mortgages. Thereby the role-over risk produced via the transformation of single mortgages with long-term maturity into short-term securities could be put aside not only to spaces off the balance sheets but also to a gullibility towards financial engineering. The construction of risk neutral special investment vehicles or entities had been central to facilitate the packaging and repackaging of such debt in the shadow banking system.

The calculation of risk relates to how banks interact (interconnectedness), their lending along economic circles (pro-cyclicality), their indebtedness (leverage ratio) and the size of banking institutions (too-big-too-fail problematique). Each source of risk has now been counterbalanced via increased capital buffers or lending and borrowing limits to be fully implemented by 2019. Even though shadow banking has often been presented as the other side of banking, the largest (investment) banks made broad usage of the arbitrage opportunities via the cash flow structure of the shadow banking system (Joint Forum, 2015; 2009).

Within the new regulatory environment and via dynamic capital requirements for banks, shadow banking practices are increasingly connected to the traditional banking sector. Via more comprehensive transparency standards for banking, their trading books and an overall leverage limit, banks' balance sheets are now more reactive to developments in financial markets. This heightened reflexivity between regulation and the day-to-day practice of banking had been brought forward via the centrality of shadow banking for modern finance. The purpose of the new regulatory environment was hence rather directed to integrate the environment of complex securitisation into common international standards than to abandon these practices all together.

The shadow banking system enables banks to manage their balance sheet in a more attractive way for their shareholders when profitability increased (FSF, 2008). It creates financial products to still high and low risk appetite through its ability to differentiate risk exposures. It combines risk mitigation strategies through liquidity facilities, credit default swaps and cash flow water falls to produce what turned out as 'pseudo-risk-less' (Stein, 2010) securities being safe in good times and highly risky in bad ones.

Indeed, securities (i.e. collateral backed financial instruments) can function as a form of money within and beyond the shadow banking system through which interconnections of the traditional and shadowy banking sector are sustained. Similar to government bonds, highly rate collateral backed securities serve as collateral for repurchase transaction as a highly liquid means for exchange of value. Thus, shadow banking opens-up a way to create debt in a seemingly very profitable and at the same time low risk way as long as the most parts of the financial system remain intact.

Though despite of the recent crisis, the failure of the shadow banking system showed the contemporary transformation of the credit system that is sustained via the post crisis approaches to make the financial architecture more resilient. The reflexivity of the shadow banking sector, in this sense, inscribes the exception of off balance sheet activities into the normality represented by the regulatory body. The implication of the present transformation of the financial system is thereby hardly one of reform regarding social and political challenges but rather one of the mechanistic necessity to keep finance functional in and of itself.

## 3.2 Calculating risk

A further force for the increasing integration of the financial field goes along with the evolution of the concept of risk. Via the modern understanding of risk as an almost reified parameter, its calculability merged different aspects of the financial field and enabled connectivities to other social realms (Beckert and Berghoff, 2013; Kessler, 2007; de Goede, 2004). The following analysis turns to the role of risk within the context of shadow banking and its regulation. The discourse on the problem of the shadow banking sector highlights the limits of risk calculations during times of systemic changes.

Such events seemingly could not be translated into appropriate risk categories by rating agencies and associated losses could not adequately dispersed via financial innovation. The 'black swan' became a sudden symbol for the limits of inductive reasoning in finance and thus of the modelling toolbox on which the shadow banking system relied. Contrary to the traditional banking sector, where central bank liquidity and regulatory capital provide certain resilience in times of unforeseen stress, shadow banking could operate in a (non)legal space of the balance sheets and hence besides regulatory constraints on leverage (Ferrante, 2015; Plantin, 2014; Ordonez, 2013).

A central driver for this evolution was the inclusion of a portfolio invariant risk conception into regulatory standards. This established a singular understanding of risk, meaning that risk can be calculated and compared independent from its locality, temporality or associated agency (Kessler and Wilhelm, 2013). Thus, 'diversification effects would depend on how well a new loan fits into an existing portfolio' (BCBS, 2005, p. 4). The respective portfolio is made up of risk-weighted assets that undergo a mark-to-market valuation. In this way, banks are asked to manage their balance sheets according to market variations in a shared governance system to keep up with the regulatory demands concerning their respective capital requirements (and profitability).

The inscription of credit ratings for financial institutions and products produced a widespread standard along which the risk structure of a bank's balance sheet could be calculated. When market developments stay within the projected range of risk analyses, credit ratings provided the 'facts', which 'suffice to determine the capital charges of credit instruments' (BCBS, 2005, p. 4). The underlying formulas to calculate the needed capital contain however intuitions about how markets should function. Though, looking at them after an event of crisis, these intuitions seem to apply only if they had not widely been built into the financial instruments aligning the banks' balance sheets to each other via regulatory 'incentives'.

One intuition in-built into capital requirements calculation is that capital charges for long-term obligations should be higher than for short term exposure. Lower capital charges for short term investments and alike investment strategies used for instance by money market funds created demand and thereby an investment incentive for an 'efficient' maturity transformation, i.e. to role-over long term investment via the issuance of short term debt by off balance sheet entities. To do so, the shadow banking system made use of collateralised debt securities which thereby were increasingly assumed to be money-like liabilities which in turn could be produced more efficiently besides the traditional and regulated banking sector (Plantin, 2014).

The notion of risk, also brought forward by joint regulatory standards, could thereby, on the one hand side, align the demand for financial products and, on the other, sustain the institutional structure able to provide tailored investment products fitting the requirements of investors and thus of internationally shared understandings of financial regulation. Shadow banking in this sense is closely related to the specific understanding of risk sustained via regulatory demands. The notion of 'enhanced risk sensitivity' provides a further perspective into the dynamism of how a shared understanding of risk enables and limits possible practices in the shadow banking sector via increasing sensitivity to the calculatory standards of risk.

The European Banking Authority points 'to "qualifying" securitisations across the hierarchy of approaches, aimed at further increasing the risk-sensitivity of the bank capital treatment of securitisations' (EBA, 2015, p. 8). Thus, the practices of securitisation shall be further included into the regulatory body assuming that thereby banks follow the product structure to be set by the regulatory authorities. This indeed affects the business model of banking and therefore also the capital flows accordingly. The statement gives further insight into the understanding of risk. It is being seen as distinct from financial products. Risk could affect them but they are themselves not understood as part of risk creation. In this sense, the sensitivity approach becomes circular if risk is itself a very product of financial markets and not an external effect.

The Bank for International Settlements complements the view on the perception of risk rather as an external effect by arguing that some financial products are inherently to little sensitive to risk pointing especially to sovereign exposures. Their preferential treatment indeed 'weakens the risk sensitivity of regulatory requirements' (BIS, 2015, p. 113). The implication of this statement seems to be rather close to the Bourdieusian argument that an increasing homogeneity of the financial field strengthens the structure of dominance already in place. The consequence of the argument above could be read as a differentiation of sovereign risk according to the compliance to the rational of the financial architecture and hence financial dominance already in place.

The European Systemic Risk Board provides a further example of how the structure of dominance is not only sustained but how it could also be more effectively inscribed into regulatory demands. In a context of differentiated sovereign risk, banks are incentivised to widen their capital basis in order to provide a more resilient balance sheet (ESRB, 2015, p. 20). Thereby the hierarchy of sovereign risk indicated before gets institutionalised via the capital structure of banks. It increases demand for 'jurisdictional safe havens' again supporting the mechanisms of dominance in place and weakening or rather excluding alternatives for financial governance.

## 4. Conclusion

This snapshot of the regulatory context regarding the practice of shadow banking provides an indicative example of the reflexive drivers in favour of increasing homogenisation. Following Bourdieu, the standard setting discourse of international financial regulation after the recent financial crisis further concentrates the resources for domination on a global scale, especially as indicated via the perpetuation of shadow banking into international capital flows. It thereby fixates the prerogative of financial rationales and excludes political contestation, which might possibly be able to question the structure of dominance in place. Indeed, the post-crisis discourse on shadow banking vividly shows how financial practice and regulation further install the pre-crisis disciplinary and political hierarchy.

The notion of risk and the institutional structure in place provide for compatibility for financial exchanges, their profitability and their regulation. The focus on new rules for securitisation sets the stage for the shadow banking system to come impregnated by the present distribution of dominance in financial markets. Policy prescriptions promoting heterogeneity to standards for financial activities are rather exceptional whereas the intentional insertion of inefficiencies as provisions for higher resilience of financial entities (i.e. higher capital ratios) seems to be exactly what is omitted by the further evolution of market-based credit intermediation.

A new contextual phenomenon in contrast to prior histories of financial turmoil is that innovation now concentrates on time rather than on space. For instance, space related offshore settings to avoid taxes seem rather echoes from the past international order even though the recent 'discovery' of the so-called panama papers provide an excellent view into past and present possibilities for ‘efficiency gains’.

Regarding time, we can observe at least two new forces, which expand (high frequency trading, Lenglet, 2011) and compress (risk calculation, de Goede, 2004) temporal horizons. The former tendency triggered a fragmentation of markets to the advantage of market operators and high frequency trading firms whereas supervisory entities are hardly able to actually understand let alone to prevent failure. The latter tendency uses accelerated computing capacity in order to run more complex risk modelling and thereby compressing more data about possible futures and open up ever more possibilities for financial innovation.

These two dynamics are complementing each other in a way, which makes more and more difficult to grasp not only the economic but also the political consequences of present financial markets. Subsequently also the new shadow banking relies on a fragile and hidden framework for financial exchange generating profits in the present and deferring possible systemic failure and hence widespread losses into a precarious future. The further evolution of shadow banking provides thus a wide opening for research into the reflexive interaction of financial innovation and regulation not as separate forces but as an intersection which indicates how financial markets express contemporary hierarchies of domination seemingly very much apart from democratic decision making about the societal location for international (shadow) banking.

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# F – Limits of critique: Civil society politicising financial regulation

The final paper points to the conditions for how financial regulation can be politicised. It argues that formalised movements of contestation align their language to that originated by the triggers for contestation. Thus, successively, they lose their critical potential. In this way, this paper has two interrelated goals. First, it reconstructs the practices of technocratisation of the European governance regime from a civil-society perspective. It thereby relates to the debate on the de-politicisation of European decision-making and connects to the literature on the (missing) democratisation of the European Union by focusing on the role of transnational civil-society movements. Second, the article highlights how the potential for critique is transformed via the present institutional structure of the European Union. Thus, critique is subject to a practice of translation, by which the potential for politicisation alters. In this way, this paper contributes to sociological discussions on translation and to the literature on the politics of expertise.

Theoretically and heuristically, it follows Callon's notion of translation conceptualised via four analytical steps: *problematisation*, *interessment*, *enrolment* and *mobilisation*. Methodologically, it draws on semi-structured interviews with representatives from civil society, trade unions and members of parliament on the German and European Union levels. Together, this paper reconstructs the changing conditions for critique regarding regulatory measures after the financial crisis and it shows how this not only impacted on the critique thereby expressed but also how this process impacted on the organisational potential and structure of movements in favour of tighter regulatory measures.

# 1. Introduction

*All information is transformation, an emergency operation on and in the Leviathan's body. (Callon and Latour 1981, 300)*

This paper explores the conditions that enable or restrict the politicisation of financial regulation. It thereby argues that formalised protest movements align to the language used in the context of concern. Thus, such movements successively lose their potential for irritation and increasingly turn to their role in aligning with the dominant subject matter. In this way, this paper associates with two interrelated debates. First, it speaks to practices of technocracy within European governance structures and the de-politicisation of policy-making in the European Union (Radaelli 1999; Seabrooke and Wigan 2016) related to the role of transnationally organised civil society movements (della Porta and Caiani 2007; Saurugger 2008; Borzel and Buzogany 2010; Mahoney and Beckstrand 2011; Dur and Mateo 2012). Second, it reconstructs how the potential for critique changes within the institutional structure of the European Union via formalised channels (Elgstrom and Jonsson 2000; Lahusen 2016). Thus protest undergoes a translational practice which changes its potential for politicisation (Callon 1986; Lenglet and Mol 2016) and reconfigures how knowledge is produced (Seabrooke and Tsingou 2014; Tsingou 2014; Adler-Nissen and Kropp 2015; Sending 2015). Spontaneous movements – often associated with specific events (Tremayne 2013) – instantiate broad relevance for their respective concerns; however, they also display a rather short endurance of existence (Calhoun 2013). Finance Watch represents such an organization that was founded in a politicised environment around the financial crisis of 2008/9, though it struggled to continue its work in a changing context, with a fluctuating internal structure and professionalization of knowledge provision. This paper analyses this transition as a case of translation (Callon 1986; Barry 2013; Tyulenev 2014).

Not only the industrial side (McKeen-Edwards and Porter 2013; Pagliari and Young 2014; Young 2014) but also NGOs and trade unions (Fioramonti and Thümler 2013a; Kastner 2014; Pagliari and Young 2016) construct a network that affects the regulatory process regarding finance. Even though the civil society network has broadened and institutionalised with the onset of the financial crisis of 2008/09 (Clark 2011; Fioramonti and Thümler 2013b; 2013a; Ford and Philipponnat 2013; Scholte 2013), it still lags its industrial counterparts, at least in terms of monetary recourses. Thus, civil society organisations established prior to the crisis did not really have any specific expertise vis-à-vis European financial regulation. Finance Watch represents this challenging context in various ways. Studies regarding civil society organisation of financial market interests show the distinguished position of this newly founded organisation especially in comparison to established non-governmental ones (Ford and Philipponnat 2013). They arrived at their expertise on Finance rather indirectly via ecological or inequality matters, and thus only had restricted knowledge about financial markets and their regulation. Finance Watch, on the contrary, specialised in financial regulation. It was founded by a network of other civil society organisations to provide a tool to produce alternative knowledge for financial regulatory matters.

Methodologically, this article relies on semi-structured interviews with members of parliaments (6) and representatives of different NGOs (6) and trade unions (4) concerned with financial regulation. One half worked on the European level the other in the German context. About half of the interviewees were active in their roles when the recent financial crisis occurred, the other half started their employment afterwards. In total 16 semi-structured interviews produced about 17 hours of interview material. Desk research about the main regulatory proposals (especially on the capital requirements for banks) produced contextual information. Thus, the article highlights the spaces between European law making, the actual practice of finance and their relation to societal sets of interests. To show the productive aspects of these spaces, the reconstruction follows the translationary heuristic developed by Callon (1986). The increasing concern of civil society groups regarding financial regulatory matters reflect a special case of emergent concerned groups (Callon 2007; Callon and Rabeharisoa 2008). Finance Watch not only employs instrumental knowledge and advocacy tools but it is organizationally also affected by it which in turn changes its activity and contextual field. Thus, Finance Watch presents an exemplar to research the 'formation of social groups and their reproduction' as its core purpose and capacity is a product of its performance and thus it is more of 'an achievement than a starting point' (Callon and Rabeharisoa 2008, 232). To display the performance of Finance Watch, the following section of the article introduces Callon's take on the sociology of translation and how it relates to knowledge production and expertise. Then, the article reconstructs the reconfiguration of Finance Watch as a network process according to Callon's four translationary phases: problematisation, interessment, enrolment and mobilisation. The final section concludes by highlighting the condition of critique, which it is always associated with its point of reference, and hence inherently limited.

## 2. Translating expertise

The recent financial crisis opened-up a perspective on kinds of politicisation and protest, both of which are directed against technocratic regulatory mechanisms. This dynamic could only partly relate to previously existing movements as a main part though they had to establish new ways to create alertness over general news media and also to 'translate' the importance of finance to further societal realms (Scholte 2013). For this, civil society organisations hold a special position in providing an alternative expertise, especially in the EU legislative procedure (Kutay 2012; Bee and Guerrina 2014). The literature on 'Europeanisation' discusses in particular their function in political socialisation for generating a European public (Warleigh 2001; Featherstone and Radaelli 2003; Della Porta and Caiani 2009). At least implicitly, it seems though that there is already a presumption of success as a condition that is inbuilt into the work of civil societies: That is the creation of a transnational political realm for a democratic alignment within the European Union. Hence this literature fails to explain how Europeanisation itself is a force which manufactures the inclusion and exclusion patterns of expert knowledge (Greenwood and Roederer-Rynning 2015; Sending 2015). A perspective which focuses on such selective practices of power related knowledge production refers to 'bricolage' to underline the situational overlay of different forms of knowledge (Engelen et al. 2010; Carstensen 2011; MacKenzie and Pardo-Guerra 2014). This means that knowledge develops historically in a specific way, though each singular event is underlined by a contingently constructed 'anomaly'.

Hierarchies of knowledge formations in international contexts have been associated with 'epistemic communities' (Adler and Haas 1992; Zito 2001) and thus the diffusion of expert knowledge in political arenas (Dobbin et al. 2007; Newman and Bach 2014; Dunlop and Radaelli 2016; McPhilemy 2016). For financial regulation, the politics of diffusion concerns transnational networks that draft and prepare regulatory measures (Bach and Newman 2010; Maggetti and Gilardi 2011; Moschella and Tsingou 2013; Seabrooke 2014; Seabrooke and Tsingou 2014; Ban et al. 2016; Seabrooke and Wigan 2016). This indicates the political aspect of knowledge and thus the production of authority within the policy fields affected. From a Bourdieusian perspective, Sending (2015, 126) shows how a field constituted out of power relations generates distinctive forms of knowledge, how they are institutionalised and finally how then political authority is sedimented. The problem of translation in the context of sociology of knowledge complements this politics of knowledge by opening up the view on the contingency of knowledge production. The sociology of translation thus allows detection of how expertise and its associated knowledge claims emerge spontaneously though conditioned by contextual power relations (Best and Walters 2013).

It is the mediating aspect between different levels of abstraction for which Michel Callon's sociology of translation offers a conceptual entrance point (Waeraas and Nielsen 2016). Then, regulatory approaches are an expression of 'structuring power relationships' (Callon 1986, 196). In contrast to institutional or cognitive readings of translation, Callon points to societal formations that can be analysed via the concept of translation. Hereby, Callon refers to a problematic relation of societal and natural events and modes of articulation. It is 'a complex web of interrelations in which Society and Nature are intertwined' (Callon 1986, 200). Thus, such an understanding of translation can focus on hybrid over-lappings of different forms of knowledge whose implications for political constellations initially rest in abeyance (Buzelin 2013, 194). One route for developing the Actor-Network perspective further points to analysing a 'broker' between different political contexts (Büttner et al. 2016). However, and in contrast to traditional analyses of civil society organisations, 'sender' and 'recipient' cannot be clearly distinguished based on successful or failed communication, though the concept of translation points to the conditional impossibility of unambiguous transmission. Indeed, it is the contingent transformation of transmission which, in the first place, allows for translation. The Actor-Network-Theory (ANT) debates how the settlement of the respective contexts of meaning becomes relevant. Discourse, language or text are thus not reduced to traditional understandings of actors but actor-hood encloses the material component of respective contexts and shows the process of constitution. That means 'creating convergences and homologies by relating things that were previously different' (Callon and Latour 1981, 211); – or as Tyulenev (2014, 166) formulates: 'Translation in ANT is recruiting actants into projects of building networks.'

Thus, the problem of politics is related to how expertise is constructed via networked processes of, in this case, civil-society formation. This discussion shows that not only the depoliticising aspect of expertise in the form of technocracy (Radaelli 1999) but also the politicisation of expertise has consequences for how power relations can be understood (Lombardi and Moschella 2016). The first aspect defers decision-making in expert fora (Greenwood 2007; Pianta 2013; McPhilemy 2016); the second aspect positions the authority of scientific knowledge as guidance in decision-making (Brown 2009; Hirschman and Berman 2014). At this juncture, the problematisation of translational relations connects the Europeanisation literature with approaches to politics of expertise. By relating both aspects, this article contributes to a heterogeneous and contingent understanding of knowledge production (Davies and McGoey 2012; Reisenbichler 2015; Ban et al. 2016) and, consequently, it allows representation of the constellation of civil society movements active in knowledge provision (Pianta 2013). To reconstruct this process of translation in detail, Callon provides four consecutive heuristical steps: *problematisation*, *interessment*, *enrolment* and *mobilisation*. The following four sections consider each step to illustrate civil-society formation vis-à-vis financial regulation. Each respective step is further outlined in its respective section and together they tell the story of how critique is transformed and, consequently, limited via translation.

## 3. Problematisation

> *You can explain everything, though only rarely someone cares*[39]

After the consequences of the financial crisis of 2008/9 became apparent, the financial reform debate also came to the fore of public concern. What has led to the situation wherein the eventual bankruptcy of a single financial institution (Lehman Brothers) led to a situation where unprecedented sums of taxpayers' money could be mobilised to stabilise the financial system? If there are such systemic interrelations, how were these forces distributed across the financial system? Which construction failures of the regulatory architecture responsible for that series of reactions could be located? Even if, for some, the vulnerability of the international financial architecture was clear, that the policy reforms regarding financial institutions and products was a case of public debate was rather unusual. The interruption of capital flows and thus the rapid losses in value and trust in financial markets affected not only bankers and traders but also the daily lives of a vast proportion of the population in developed and globally interconnected countries. Private and public institutions experienced unprecedented pressure over their decision-making without a clear understanding of the reasons for this situation.[40] The problem of lacking information about the financial system and its daily practices relates to how information was generated. The previously accepted routines of supervision and transparency were called into question. Such a situation demanded or enabled a revision of the financial architecture then in place. At the same time, the need for justification within the political arena grew. Elected parliamentarians now had the responsibility to explain the origins and triggers of

[39] Interview, Member of the European Parliament, 20 November 2014 (#12).
[40] Interview, Member of the German Parliament, 16 July 2014 (#01).

the financial crisis to their electorate.[41] They felt an urge to explain why public money could be used for the banks and a financial system in crisis, though it had not been available beforehand to increase social security, improve education or cutting taxes.[42] Trade unions and other civil-society organisations were now interested in the details to support a more stable financial architecture.[43] Such political momentum was not directed towards financial regulation before. Indeed, previously apparent crises were often associated with other regions and not the highly-industrialised society of Western states.[44]

Despite the broad media attention given to finance, it was still difficult to communicate technical details beyond expert circles. Exceptions to this were the bonus cap, the financial transaction tax or matters involving food speculation[45]. These aspects pointed, however, to either a general pejorative attitude towards bankers[46] or were connected to more established critiques of inequality.[47] For instance, only after the details of capital requirements for banks were agreed upon within international expert for a could the European Parliament decide on the results (not contents), which subsequently were implemented in national law. The technical aspects (apart of the bonus cap which is not immediately related to capital requirement legislation), e.g. risk categories, transparency or systemic risk reduction, were not part of the public debate. This was reasoned at the same time via the abstractness[48] (as there were no immediate effects for the public) and the concreteness [49] (as politicians are not experts themselves on the respective policy matters) of financial regulation.

Until the financial crisis, the main international bodies for regulatory issues had no public relations unit. Existing access points to information had been reserved for experts of the institutions to be regulated.[50] The technicalities of the discussion could not practically be politicised before the crisis, and hardly thereafter, because it was unclear how financial regulation related to other societal fields. There were no routines for 'translation' in place. Established procedures allowed for the participation in hearings regarding regulatory issues and thus, potentially, for rather limited excess points for public discussion. Hence, on the one hand side, there were possibilities for a diverse discussion on central regulatory efforts; on the other hand, this openness had

[41] Interview, Member of the German Parliament, 24 September 2014 (#04).
[42] Interview, Member of German Parliament, 16 July 2014 (#01).
[43] Interview, trade unionist, 12 November 2014 (#09).
[44] Interview, NGO representative, 23 September 2014 (#03).
[45] Interview, NGO representative, 23 September 2014 (#03).
[46] Interview, trade unionist, 12 November 2014 (#06).
[47] Interview, NGO representative, 23 September 2014 (#03).
[48] Interview, trade unionist, 13 November 2014 (#10).
[49] Interview, Member of European Parliament, 02 June 2015 (#16).
[50] Interview, NGO representative, 12 November 2014 (#08).

a structuring effect on the regulatory debate, as well as for the public more generally. Public hearings provide a very formalised format which limits the range of problems and issues for comments. Beyond that, the financial and scientific possibilities are unevenly distributed on the participants' side. This means that the affected financial industries affected have qualitatively different means at their disposal. This has been shown very clearly, especially for the financial sector (Pagliari and Young 2014).

There has been a heightened demand for professionalisation because of the interaction of regulatory agencies with civil-society organisations and the need to participate in the regulatory discourse.[51] Such expertise, however, goes hand in hand with the problem that critique is increasingly to be inherently formulated. This means that critique is related to the existing regulatory approaches and disentangled from broader political orientations. Then, problematisation thus focuses on the available access points for civil society actors and for the decision-makers in parliaments. Experts and their language thus represent an 'obligatory passage point' (Callon 1986) for the work of civil society regarding financial regulation. The political malposition, that expert knowledge is hardly available apart from financial industry efforts culminated in the creation of an organisation that made 'making finance serve society' its principal cause. This, however, raises a challenge to relate different societal groups via the topic of finance. The following section shows how the needed *interessment* turned out in the field.

## 4. Interessment

*Finance Watch is an amazing help*[52]

Building on *problematisation*, as outlined above, we can now look at the central restrictions on politicisation regarding financial regulation. The restrictions are there to translate argumentations across different policy arenas, though in a fundamental manner. It is not only that different jargon is used but also that how arguments make sense in respective fields differs. This epistemological divide between policy areas is a main obstacle, i.e. to render financial knowledge relevant to other participants of the debate and, at the same time, to keep the line of argument intact. NGOs provide resources for analysing financial markets and to find out about the mechanisms via which they

[51] Interview, NGO representative, 12 November 2014 (#07).
[52] Interview, trade unionist, 13 November 2014 (#10).

relate to their respective core themes (WEED 2010; Brot für die Welt 2014; DGB 2014). Exemplary for this is research funding, new staff positions or the creation of new forums for networking[53]. By looking back at original efforts, it is represented as difficult to make this organisational structure permanent as the crisis experience lies further in the past.[54] The 'obligatory passage point', as highlighted by Callon, is thus to create a narrative which reasons the permanent need for knowledge regarding finance by respective NGOs, and thus for other societal realms. Finance Watch positioned itself as such a node which, on the one hand, provides specific knowledge and, on the other, tries to find concerns shared with other policy arenas. Indeed, members of the European Parliament initiated Finance Watch because of the need for alternative knowledge regarding the industry's expertise. Other NGOs in turn understood the need for more substantial information about how to intervene in the process of regulating financial markets.

Thus, Finance Watch served as a catalyst to relate the interests of different civil society actors. This is what is termed as 'a variety of techniques of getting the actants interested' (Tyulenev 2014, 166). Such interessment found that a variety of different civil society bodies could formulate their respective interests in favour of a stable financial system. Only a few of these actors had the know-how to participate in the debates on regulatory proposals; and if so, only in restricted areas, e.g. workers' rights or consumer protection. Trade unions, consumer groups and other NGOs indicated their need to have access to financial knowledge from a practitioner's perspective. However, such knowledge should be opened up to a broader understanding to enrich the public discussion regarding financial regulation. It was about how knowledge could be presented that was meant to interrelate between different actors in the field. Finance Watch thus serves as a particular epistemic device, which (akin to Callon et al. 2007, 2) 'denotes material and discursive assemblages that intervene in the construction of' not only markets, but also in the generation of knowledge. The main property of such a device was that it could relate to different policy languages of civil-society networks (and their respective core topics) of the financial sector, and their routines, as well as politicians and policy. In a sense, the regulatory debate, which was the main consequence of the financial crisis after the failure of Lehman Brothers, should not have been left to the experts deemed responsible for wrong regulations in the first place. For this, on the one hand, a distinctive juridical and economic

[53] Interview, trade unionist, 13 November 2014 (#10).
[54] Interviews, Member of European Parliament, 20 November 2014 (#12); NGO representative, 19 May 2015 (#15); NGO representative 12 November 2014 (#08).

knowledge was to be mobilised;[55] on the other hand, it was to be connected to core NGO work, e.g. regarding how to organise a campaign based on these critical interventions.[56]

In times of crisis, the European Commission as well as the European Parliament could be convinced to financially support an alternative body for generating knowledge about financial regulation. In addition, a European network of civil-society groups supported the creation of Finance Watch, and also having access to such knowledge on an ad hoc basis. Especially in the first year after the Lehman bankruptcy, there was this special need with respect to the very large number of regulatory proposals to be decided on – 'there had been so much'.[57] Financial expertise after the inception of Finance Watch was only a call away. Regular meetings of Finance Watch's stakeholder group allowed for the inclusion of societal areas according to their respective interests regarding finance as well as regulatory implications. Via a newsletter, a specific circle is kept informed about present challenges regarding regulatory changes and this has effects beyond the financial sector. Beyond that, a network of experts working for NGOs with specific expertise in finance crystallised. These parts of the network inform, invite and amplify each other. Research-oriented institutions collaborate with Finance Watch to clarify the socio-economic implications of changing regulatory matters. Research on Finance Watch contributes to its singularity in the field of financial regulation from a non-corporate perspective. Finance Watch also created an alternative space for practitioners during and after the financial crisis. People previously working in the financial sector accepted lower salaries to work for this NGO.[58] The new reform agenda for the EU financial system allowed their often newly appointed staff the opportunity to take part in substantial regulatory reform. For this, public consultations provide an inclusive mechanism to comment on regulatory proposals and thus the formal eligibility to influence the policymaking process. This creates a common focal point for interest groups regarding when and how to intervene in specific regulatory reforms.

The founding moment related to the post crisis regulatory challenges created a common interest for NGOs and politicians to set up a new institutional configuration called Finance Watch. It worked as an epistemic device that relates different strands of knowledge formation. Via its translatory capacities, it thus related different policy fields and formed a common node for influencing financial regulation from a non-corporate perspective. It was at the centre of *interessment*, which kept people together by demanding for and

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[55] Interviews, Member of the European Parliament, 02 June 2015 (#16); Member of the European Parliament, 20 November 2014 (#12).

[56] Interview, NGO representative, 23 September 2014 (#03).

[57] Interview, NGO representative, 13 November 2014 (#11).

[58] Interview, NGO representative, 12 November 2014 (#08).

delivering resources. The next section shows how this foundational moment is succeeded by *enrolment*, meaning the stage of creating a more institutionalised framework which, in turn, allows the network to continue at times when immediate crisis dynamics lessen their prevalence.

## 5. Enrolment

> *…we are working on it because it was in the Commission's proposal.*[59]

Along with participation in the official procedures of financial reform, the space for available action is affected by how the regulatory problem is framed. The work of civil-society actors in financial regulation cannot always rely on public relevance due to crisis dynamics, but it also adapts to the procedural context within which critique and regulatory changes can be articulated.[60] Some aspects that represent the increasing consolidation of the institutional field can be observed via changing financial support for Finance Watch, or the increasing distance expressed by people involved from the start. The expression of 'the last crazy year'[61] indicates how the intensive phase of initial work is substituted by consolidation. In comparison to established routines, the initial phase of improvisation, a high work-load and excitement, is distinct. This change also applies to the new European Commission. Thereby, reactive measures to regulate the markets (via new capital requirements or the Banking Union) turn now to proactive measures (like the Capital Markets Union). The letter stance questions the measures regarding restrictive credit provision established for fear of building up further financial bubbles and it instead tries to reinstall a more expansive regulatory context for financial institutions and products.

Following the Lamfalussy procedure, a further contextual transformation is the different levels within which the initial reform endeavours are discussed. As the general rules are settled via directives and regulations (Level 1), the post-crisis regulatory measures in Levels 2 and 3 discussions are far more technical and routinized than it was the case before. At this point the discourse is directed towards practitioners and firms in the financial sector as it is about how to make the general rules feasible for daily financial practice. This is where public consultations take place organised by the four main

[59] Interview, NGO representative, 12 November 2014 (#07).
[60] Interview, NGO representative, 12 November 2014 (#07).
[61] Interview, NGO representative, 12 November 2014 (#07).

newly-created supervisory agencies for observing the re-regulation of financial markets in the European Union (European Systemic Risk Board, European Banking Agency, European Insurance and Occupational Pensions Agency and European Securities Markets Agency). In this context, it is about the application and implementation of the regulatory setting as well as a discussion of the revisions needed to make the broader regulatory measures work. When the European Parliament or Council discusses about the general setting of financial regulation, it is much easier to relate these issues to broader public concerns whereas the technical level of regulatory discussions is far more specific to the businesses involved. Nevertheless, changes on non-level 1 also affect the broader reliability of the financial architecture.[62] The arguments required to make technical debates relevant to 'real world' experiences become more complex. Thus, the civil-society network for financial concerns also needs to adapt its workflow. The most general instantiation is the increasing needs to be close to the respective debates by being present in Brussels.[63] More specifically related to Finance Watch, it involves its focus on employing practitioners and lobbyists from the financial sector to be able to relate to relevant financial regulatory debates.[64]

Thus, Finance Watch – as a central hub for providing financial expertise – established itself in the Brussels NGO world. This, however, has two consequences. On the one hand, Finance Watch gained knowledge about how to intervene efficiently in legislative procedures; on the other hand, and at the same time, this reduced its potential to influence the regulatory agenda. Indeed, Finance Watch may function as a symbol, which then can also be used as an 'alibi',[65] in the sense that if Finance Watch participates in consultations or debates, the interests of civil-society are considered to be heard and consequently incorporated into the resulting regulatory outcomes. Callon (1986, 205–206) terms this stage of translation *enrolment*. He understands it as the constitution and acceptance of a problematic field. The field is also known regarding the limitations for influencing procedures therein. What is also indicative when looking at financial regulation is that the consolidation of relevant actors leads to a different dynamic within the organization and regarding its external relations. To keep the quality of the staff or to sustain relations with donors and other NGOs, Finance Watch moved from being a project of NGO representatives and trade unionists to being an institution employing and serving people. Thus, the scope of its action is also affected. The crisis

[62] Indeed, what can be observed recently is that the lobbying process is focussing more on Level 1 discussions, which makes these measures more detailed and technical, so that blockages can occur, which in turn delineate the scope of implementation on Levels 2 and 3.

[63] Interview, NGO representative, 13 November 2014 (#11).

[64] Interview, NGO representative, 12 November 2014 (#08).

[65] Interview, NGO representative, 12 November 2014 (#07).

mode made it easier to relate regulatory matters and broader societal perspectives, whereas, without the grand narrative of unstable financial markets, connecting civil-society agents to critique regulatory changes becomes more difficult. Thus, this translatory stage highlights the problems of politicising financial regulation when routines are dominant again. Whereas the fine-tuning of regulatory matters is of interest to industry representatives as it affects their business models, the economy of civil-society bodies depends on how the societal implications of their work are perceived. This in turn also depends on the economy of their topics and not only on their concern.[66]

In crisis mode, for instance, revision of the directive on markets in Financial Instruments (MiFID II) could relate to food speculation or disclosure requirements related to retail markets. The case of the revision of the capital requirements directive and regulation (DRR/CRD IV package) showes how politicisation was made possible by adding a popular policy to it. The bonus cap was not foreseen as part of the capital requirements regulation, but the European Parliament could make a case to add policies to the pre-formulated Basel Agreement. However, if measures like capital-requirement calculations regarding risk categories for specific financial products cannot be related to broader societal interests, it becomes more difficult to sustain the supporting civil society network and thus to generate the resources needed for continuous regulatory work. *Enrolment* is the stage where network routines can be established and which can be activated based on need within respective regulatory contexts – be it via spontaneous telephone calls, comprehensive reports regarding regulatory measures or regulatory meetings of the civil-society network connected via Finance Watch. This stage also shows that there is an understanding of what kind of tools are needed, when there is a demand for them and how they can be provided. Thus, the effect was the strategic usability of the network in different regulatory settings, to react to specific reform agendas and finally also to coordinate proactive measures. It is only at this stage, that this network can be *mobilised*, as outlined further in the section below.

## 6. Mobilisation

*At some point, it will always crash again.*[67]

[66] Interview, NGO representative, 12 November 2014 (#07).
[67] Interview, Member of the European Parliament, 20 November 2014 (#12).

After the high number of new regulations, the inception of new regulatory agencies and other revisionary measures, new resources as well as restrictions also structured the field for civil-society engagements. The new 'mobility' allowed for developing new positions, but it came with less pressing demands and thus diminished relevance in daily policymaking routines. Finance Watch as an organisation could move more independently; however, this came with more difficulties to sustain their funding resources. Such *mobilisation* may thus come with qualitative differences for the network structure (Tyulenev 2014; Waeraas and Nielsen 2016). Thus, *mobilisation* for Callon (1986, 196) means 'to ensure that supposed spokesmen for various relevant collectivities were properly able to represent those collectivities and not betrayed by the latter'. Finance Watch could take such a speaking position within a well-defined problem area. This means that Finance Watch has an original position for addressing questions of financial regulation that are relevant to broader societal areas, and thus for a broader network of civil-society actors. An ongoing problem with such *mobilisation*, however, is the 'stand-by' mode that stands in contrast to the exceptional situations during crises, which come with continuously pressing needs. The quote by Callon ('to ensure that… ') can thus be read as a straightforward imperative for developing a sustainable network architecture related to its specified function, if the network setting is not being lost.

The campaign in favour of the financial transaction tax and the discussion about the restriction on bonus payments could relate to a variety of existing inequality discourses. Their actual point, to improve the general setting for financial regulation, might have only been a minor issue for the public relevance. For inequality issues, especially regarding the financial transaction tax, civil-society networks had long been in place and could be activated to support this policy proposal that had been discussed for a long time, but which gained a new momentum during the regulatory discussion with regards to the crisis dynamics.[68] Also, the debate on the bonus cap did not come naturally out of the regulatory discussion. The major banking-reform measures in the form of the Basel III did not entail such policy recommendations. Such politicisation could only be introduced literally in the last moments of the policy decision in the European Parliament.[69] Politicisation was thus more an issue of 'grafting', in contrast to a confined evolution of regulatory measures. This experience very much questions how a *mobilised* and thus self-sustaining network architecture of civil-society organisations explicitly relates to financial regulation that can be transferred into institutionalised contexts independent

[68] Interview, NGO representative, 23 September 2014 (#03).
[69] Interview, NGO representative, 12 November 2014 (#08).

of acute crisis dynamics. Thus, the question remains of whether specific expertise in technical details regarding financial regulation can be translated into a continuous institutional structure.

In this way, it is the focus on the regulatory process of financial regulation that constitutes the main strength, but also a major weakness, for sustainable *mobilisation*. This direction makes such a network highly dependent on the 'supply' of regulatory problems, whereas the 'demand side', due to the restricted area, cannot be sufficiently developed. Such a context for politicisation opens up a paradoxical relation. On the one hand, there is the possibility that fluid protest movements could be developed during the recent financial crisis (such as the occupy movement), which also contributed to increased interest in financial and regulatory technicalities; on the other hand, however, such protest movements were not able to access regulatory procedures in an ad hoc manner, as 'it is very complex to enter the financial regulation debate'.[70] *Mobilised* networks, which gained their position because of how they confronted societal problem areas and the way financial regulation is calibrated, are thus also dependent on routines which can hardly be translated into a language for *mobilisation*. Formalised organisations adapt their language to the object of resistance and thus lose the critical potential which comes with more fluid protest movements. The translation and transformation of interest constellations change the political body of the organization itself and thus establish new possibilities but also restrictions.

The production of specific knowledge to take part in the regulatory debate should be complemented with knowledge about the access points to the policy-making process, as well as to relevant civil-society actors. It is exactly this more ambitious outlook which on the one hand has the potential for initiating policy change but, on the other, points to the need self-transformation to reach such a position. Knowledge is thus not only a resource which can be harvested and nourish already present needs. Knowledge generation and its application go hand in hand with a changing institutional essence of involved and related agencies. Thus, even though knowledge is needed which not only allows for influencing the regulatory process but which also enables changing the playing field, this process of knowledge generation affects also underlying interests, policy goals and political relations. *Mobilization* serves these dynamic but it is also a representation of how the translation to reach this stage transformed the original body and its associations within a state body more broadly. *Mobilization* may thus allow creating a sustainable position within a post-exceptional environment, but 'all information is transformation, an emergency operation on and in the Leviathan's body' (Callon and Latour 1981, 300).

[70] Interview, NGO representative, 12 November 2014 (#07).

## 7. Conclusion: Limits of critique

Following Callon's heuristic for processes of translation, this article reconstructed the establishment of a civil society network regarding questions of financial regulation. The first step, *problematisation*, gave an overview about challenges posed by the Great Financial Crises for civil-society networks. The second step, *interessment*, was especially triggered via the crisis mode and established strategies for impacting on the process of related financial reform. The third step, *enrolment*, indicates the forces which contributed to and challenged network relations within the civil-society movement. Relations seemingly established, were disentangled again. In the fourth and final step, *mobilisation*, the network was disassociated from the prior operation mode of crisis. Now, the civil-society network is confronted with new demands to establish its own strategies for politicisation regarding financial regulation. Such efforts may indeed be useful to work proactively and influence regulatory decisions from the start; however, via this specialisation and association regarding the regulatory process, the critical potential decreases along with an increased adaptation of the language to its object of critique. Thereby, this contribution points to the preconditions that allow and restrain politicisation. Formalised protest movements, which take an active part in the policy-making process, also entangle themselves with the regulatory routines provided. Such mobilised counter-movements successively lose their prior critical potential, but they also establish functional tools to affect the regulatory process, which are not present in more spontaneous and fluid movements. Especially within the European Union, contestation regarding financial markets increasingly adapts to formalised measures to have an impact on policymaking.

Two aspects may be highlighted along with the analyses of interviews with trade unionists, civil society representatives and parliamentarians. First, the effectiveness of protest related to affecting respective political communities seems increasingly be directed to lobbying work in the process of policymaking. The example of the financial transaction tax is an example of politicisation via already established civil-society networks. Second, there is an increasing relevance for civil society organizations to provide their 'own' expertise within the respective policy fields. For financial markets policies, Finance Watch has been established as a central producer of alternative, non-corporate knowledge. The indicated example of civil-society organization expresses the limits of effective politicisation. It shows how the articulation of protest within formalised policymaking procedures also changes the content of critique. Despite far-reaching preparations regarding the financial transaction tax, for instance, the related campaign has slowed down. The politicisation of reforming capital requirements for banks was only partly successful via discourse grafted on related to the bonus cap. One problem from the beginning was the missing technical expertise for the lobbying process regarding financial markets' regulation. This had only to be established.

The emergency operations of the Leviathan were in full swing during and shortly after the crisis. Political positions were newly adjusted and the sustainability of the implemented measures is now on probation under normalised conditions. The sociology of translation that allows us to follow this process enables to understand the structure of the network for politicisation and creation of resistance, as well as for overreaching authority in the field of financial regulation. In contrast to traditional analyses of civil-society organisations, which tend to analyse the relation between sender and receiver as being either successful or not, the concept of translation assumes the principal impossibility of unambiguous transmission. Translation by relating different contexts does so in a contingent way. It confronts interpretations with existing network formations. These relations, though conditioning the way of translation, also open up unlimited possibilities for adaptations. New protest movements are in a state that is similarly constituted and spontaneous. They may already have the potential to take part in rather formalised way to influence policy via a variety of technological possibilities. A main access procedure, though, concentrates on the formation of alternative expertise, even including simulating experts already in place. However, such protest movements adapt to the policy world and thus they may lose their initial connectivity to their foundational constellations.

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# G – Outlook

*We define shadow banking activities as banking intermediation without public liquidity and credit guarantees (Adrian and Ashcraft 2012, 101).*

Following this quote by Adrian and Ashcraft and from today's perspective shadow banking has ended via its new connections to public resources. From today's perspective shadow banking is supported by a new regulatory environment (for instance regarding money market funds) and by new liquidity tools of central banks (for instance by buying mortgage backed securities). In this respect, regulation regarding shadow banking ended with (at least structurally) 'enhancing supervision and regulation of the shadow banking system in areas where systemic risk and regulatory arbitrage concerns are inadequately addressed is therefore important' as it has been called for by the Financial Stability Board (FSB 2011, 1). Shadow money, i.e. privately originated money-like financial products intermediated 'without public liquidity and credit guarantees', however, is a continuously renewing process of financial innovation (Pozsar 2016).

The 'new normal' of the 'monetary institutional form' comes along with new social, political and economic hierarchies with respect to how value is constituted, legitimized and distributed. With respect to the regulation of shadow banking especially the so-called macro prudential paradigm gained prominence (Baker 2013). This regulatory agenda instantiates an 'effort to control the social costs associated with excessive balance sheet shrinkage on the part of multiple financial institutions hit with a common shock' (Hanson et al. 2011, 5). From a socio-political perspective, it provides a frame within which social problems can be governed from afar. Such remote control preconditions, i.e. restricts and enables, local situations which in turn rise concerns for coordination on the macro level (Thiemann and Lepoutre 2017). In the aftermath of the financial crisis three aspects seem to be central for understanding the change of the financial system and its governance: the new normal enabled a new frame for *seeing (financial) markets*; it provided the ability to capitalize on the new regulatory framework via readjusting *market-based business models*; and financial institutions gained new technological capacities to renegotiate the spheres of *automation and judgement*.

*Seeing (financial) markets*: Markets can be positioned as a prism through which socio-political reality can be understood, i.e. as a powerful interpretation of social processes and their alliances to certain routines (Lenglet 2012). These routines, however, are not foundational but themselves observed, ruled, constructed, reformed or short regulated. The 'fear of debt'

(Fourcade and Healy 2017, 26) does not come from the market but from the way how the market is instrumentalized. The creditor/debtor relation, i.e. who should fear whom, is thus contingent on the regulation in place: it is a 'conflict-ridden distributional exercise' (Carruthers 2015, 390). Thus, markets are not spontaneously and neutrally established devices of reorganization but legal instruments for distribution. To read regulation provides the analytical perspective for understanding the distributional conditions and implications.

*Market-based business models*: As power-laden strategies for governance, markets are increasingly used to structure large volumes of information as provided by present digital technologies (Fourcade and Healy 2017). This brings about new access to informational networks and thus cheaper products which can accustom more specific needs – the insurance sector being a prominent instance for harvesting the new amounts of consumer data to customise their products (McFall 2017). The Fintech industry instantiates another new evolution in providing financial services at low cost for a large amount of 'users' which can indeed also serve as a development policy tool providing finance to the 'unbanked' (Gabor and Brooks 2016).

*Automation and judgment*: The growing importance of algorithm based financial interaction provokes new challenges for regulation not only in scope (Coombs 2016) but also in the language applied. Whereas traditional regulation was meant to specify procedures between humans for instance via paper work (Preda 2002; Riles 2010) and thus giving a space for interpretation, algorithms as automated interaction demand for regulation with a comprehensive frame for their potential execution, for the effects of their interaction with each other and, arguably even more complex, their legitimate interaction with humans (Arnoldi 2016).

All in all, politics of financial regulation is about the condition of possibility of decision-making, which is logically prior to what politics is usually denoted as. It is the latter aspect that served as the pivotal theme of this dissertation and it showed how politics is powerfully limited thereby for the better or worse. The role of financial regulation in general, and shadow banking regulation in particular, is thus of central importance when it comes not only to orchestrating large financial flows across the globe but also when it comes to the 'financialised' deliberation what value is actually about (Chiapello 2015). However, whereas the socio-political implications in resent developments for financial markets and banking has been very well researched, especially in Economic Sociology and in International Political Economy, the implications of future imaginaries inscribed into the present setting of rule and rules is still to be explored further as singular examples indeed show (Palan 2014).

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